STATE OF VERMONT
PUBLIC SERVICE BOARD

Docket No. 7270

Joint Petition of Verizon New England Inc., d/b/a Verizon Vermont, certain affiliates thereof, and FairPoint Communications, Inc. for approval of an asset transfer, acquisition of control by merger and associated transactions	)))))	Hearings at Montpelier, Vermont September 5–7, 17–21, 2007

Order entered: 12/21/2007

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John D. Burke, Board Member
David C. Coen, Board Member

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I. INTRODUCTION

In this Order, the Vermont Public Service Board ("Board") denies a petition, filed jointly by FairPoint Communications, Inc. ("FairPoint") and Verizon New England Inc., d/b/a Verizon Vermont ("Verizon"), under which FairPoint would acquire the Vermont local-exchange and long-distance businesses (and related assets and operations) of Verizon.[2] If not for the financial risks associated with the transaction, we would approve the merger, subject to a series of conditions that we would find necessary to ensure that the transaction would promote the public good and not impair competition.

Notwithstanding the many appealing elements of allowing FairPoint to replace Verizon, the evidence raises significant questions about FairPoint's financial soundness as it seeks to operate the newly-acquired territories in Northen New England — a service territory that has five times the number of access lines as FairPoint's entire present operations. In particular, FairPoint's financial projections fail to take into account risks that have the potential to lead to a reduction in service quality, to less investment in the Vermont infrastructure, and to slower deployment of broadband services than is acceptable. Put simply, FairPoint has not shown that its operating units in Vermont will have sufficient funds to meet all capital and investment needs (including broadband-deployment needs) and achieve established service quality standards.

We are persuaded that the proposed acquisition offers potential benefits to the Vermont customers now served by Verizon: (1) improved service quality; (2) expansion of broadband coverage to reach over 80 percent of Verizon's current customers, along with faster speeds; (3) a commitment to make adequate investment in the infrastructure; (4) expanded service offerings;

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2. In this Order, we use the term "Verizon" to refer to the company operating in Vermont: Verizon New England, Inc., d/b/a Verizon Vermont. References to Verizon's affiliates or the parent corporation will explicitly refer to that entity. References to FairPoint are to the corporation that seeks to acquire Verizon's properties within Vermont.

Under the proposed transaction, FairPoint would also acquire the Verizon local-exchange and long-distance business in New Hampshire and Maine. Joining Verizon in this petition are also the following Verizon affiliates: NYNEX Long Distance Company ("NYNEX Long Distance"), Verizon Select Services Inc. ("VSSI"), Bell Atlantic Communications, Inc. ("BACI"), Northern New England Spinco, Inc. ("Spinco"), Northern New England Telephone Operations Inc. ("Telco"), and Enhanced Communications of Northern New England, Inc. ("Newco") (we refer to Verizon, these affiliates, and FairPoint jointly as the "Petitioners"). The proposal involves a number of steps, culminating in the sale of a portion of Verizon to FairPoint and the merger of that unit into FairPoint. In this Order, we have generally described the acquisition as the "Proposed Transaction" or "Merger."

and (5) the presence of a company whose major interest is providing wireline telecommunications service in Vermont and the other northern New England states. Because of these potential benefits, we remain open to a new filing from FairPoint that seeks to address the financial concerns that we describe in this Order. To assist FairPoint, the Order also discusses in detail the non-financial conditions that would apply to any approval we may subsequently grant; we have specifically delineated the conditions we would adopt throughout this Order and in Appendix B.[3] We will leave this docket open to permit FairPoint to submit additional filings to address our concerns.

The sale of Verizon's Vermont service territory to FairPoint would have a significant impact on the many Vermont consumers. Verizon is the dominant telephone company in Vermont, a status it (and its predecessors) has held since the early days of telephone coverage. It serves about 85 percent of the land telephone lines in Vermont, although the number of customers it serves has declined due to the advent of competition from wireless and other providers.

FairPoint plans to be a wireline telecommunications company with over 80 percent of its customers in Vermont and the other two states of northern New England. For FairPoint, these states are where it will want to expand its broadband offerings and to invest its capital so as better to compete with cable and wireless providers. In fact, expanded broadband service and the associated revenues are essential to the success of the proposed transaction. As a result, FairPoint has committed to deploy broadband service that, for many customers, will exceed the speeds provided by Verizon's service; FairPoint also hopes to surpass Verizon's current mandate to make Digital Subscriber Line ("DSL") service available to 80 percent of its Vermont customers by 2010, by meeting the 80 percent threshold a year earlier and, it hopes, by pushing availability closer to 88 percent.

Because it views itself as a rural wireline company, FairPoint also has strong incentive to provide good service in Vermont; it has committed to plans that will help it meet service quality standards and address other localized service quality issues. During hearings, FairPoint's

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3. As we do not now approve the transaction, we do not adopt these conditions in this Order. Appendix B contains the conditions that we would expect to incorporate into any order approving this transaction.

managers demonstrated technical competence to provide quality service to Vermont consumers. Moreover, FairPoint's planning for the transition of services appears to be well managed. Overall, we have been persuaded by the sincerity of FairPoint's managers who testified, and we have concluded that FairPoint will make greater efforts than Verizon to provide Vermont customers with high-quality services and to keep them as subscribers.

By comparison, Verizon has made clear that it is less interested in operating a wireline telecommunications company in rural areas. Instead, its interests have been directed more to wireless service and the deployment of new fiber-to-the-home systems in suburban areas. Vermont has experienced the effects of this change in Verizon's priorities. As we have discussed in previous orders, the deployment of DSL broadband technology in Vermont was delayed for a number of years, beyond when Verizon had led the Board to believe it would be deployed.[4] Even now, only approximately 65 percent of Verizon's customers have access to DSL, accomplished in part through our decision to allow Verizon to collect substantially more in rates than we would normally.[5] Verizon also has no plans to deploy in Vermont broadband services beyond DSL (such as fiber-to-the-home) as it is in other states. Verizon has violated at least one service quality standard every year since the adoption of the standards in 2000, and has consistently failed to meet the standard for repair of residential troubles. Verizon also has apparently deferred outside-plant maintenance so that "double poles" are now a statewide problem. Over the same time period that these service quality degradations occurred, Verizon reduced its workforce in Vermont and elsewhere among the workforce that provided services to Vermont. The workforce reductions may well have a causal relationship to these service quality and plant maintenance problems.

On balance, FairPoint's proposal appears to be preferable to the continued presence of Verizon in Vermont. However, both FairPoint and the transaction present significant risks for Vermont customers. The transition itself is a massive and complex undertaking, with the potential for incorrect bills, delays in service provisioning, customer inconvenience, and even

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4. Docket 6959, Order of 9/26/05 at 18–19.

5. Dockets 6959/7142, Order of 4/27/06 at 1–2, 17–18. Pursuant to the Incentive Regulation Plan, Verizon is required to extend its broadband service to 65 percent of its customers by the end of 2007.

service disruption. FairPoint's efforts, coupled with several conditions we discuss in this Order, should minimize these risks.

Of greater concern is the fact that FairPoint's ability to provide the benefits discussed above depends upon it having sufficient financial resources. Here, the evidence raises significant questions. The proposed three-state transaction will lead to FairPoint taking on $2.5 billion in debt. FairPoint must continue to generate sufficient revenues to service this debt as well as to fund dividends for its shareholders. FairPoint has presented cash-flow projections showing that it expects its revenues to be adequate, with a substantial margin. Nonetheless, these financial projections of operating costs, capital expenditures, and revenues (which incorporate the effect of line losses due to competition) also suggest that under reasonably foreseeable circumstances, FairPoint may face a difficult choice between maintaining a dividend to its shareholders and spending the money on operating expenses; FairPoint may even be unable to generate sufficient money to meet its large debt obligations.

Significantly, the risks associated with these uncertainties do not rest solely with shareholders or debtholders. As presently structured, FairPoint could be in a situation where, either by choice or as a necessity to meet debt obligations, it would need to reduce operating expenses, slow expansion of broadband and other services, and reduce investment to enable it to continue transferring money from the Vermont operation to the parent company (and on to shareholders). Such an outcome would adversely affect Vermont consumers, in the same way that Verizon's workforce reductions appear to have led to poorer service quality.

It is certainly *possible* that FairPoint can perform as it hopes and generate adequate revenues. Nonetheless, to date, FairPoint has not demonstrated that the risks to Vermont ratepayers are acceptable.

Before we can grant approval, FairPoint will need to address these financial concerns. In particular, FairPoint must demonstrate that the operating company will continue to have sufficient funds to meet operating expenses and capital requirements even if the risk factors we identify in this Order occur. The record does not provide adequate information for us to specifically delineate how FairPoint would meet these requirements or whether there are conditions that we could adopt that would address our concerns. It is possible that FairPoint could alter the current arrangements or develop adequate protections. These may include elements such as restrictions on the payment of dividends from the operating companies to the parent or from the parent to shareholders, reductions in the size of the expected debt service, reductions in the purchase price,[6] or some other mechanism (or combinations).

If FairPoint seeks to address our financial concerns, it should do so in light of the specific conditions that we would adopt. This includes the "consistent coverage" broadband expansion plan proposed by the Department of Public Service ("Department" or "DPS") that is designed to ensure that at least half of Verizon's present exchanges have broadband service available to all customers. The Department's proposed deployment, coupled with the efforts of the Vermont Telecommunications Authority, would likely lead to a higher total availability of broadband within the state than would FairPoint's proposal alone.

II. Procedural History

A. Petition

On January 31, 2007, Verizon, FairPoint, and several Verizon affiliates (collectively, "the Petitioners") filed a joint petition, under 30 V.S.A. §§ 107, 109, 231 and 311, seeking an order approving the transaction pursuant to which FairPoint would acquire Verizon's local exchange and long distance businesses in Vermont. A prehearing conference was held on February 23, 2007, and a memorandum order was issued thereafter setting a schedule in this docket.

B. Interventions

We granted permissive intervention to the following parties:[7]

- The Communications Workers of America and the International Brotherhood of Electrical Workers (collectively, "Labor Intervenors" or "Labor");

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6. On December 13, 2007, FairPoint filed with the Board a copy of a settlement agreement that it had reached in the Maine proceeding with some parties, including the Maine Public Advocate. This agreement included conditions that had the effect of lowering the purchase price of the acquisition. This settlement was not filed for our review and approval and, accordingly, we have not considered it in this Order. As a result, we expressly take no position on whether the changes embodied therein may address our concerns.

7. Orders of 3/28/07 and 6/6/07.

- The Eight Independent Telephone Companies (collectively, the "Eight Independents"), consisting of Shoreham Telephone Company, Inc., Topsham Telephone Company, Inc., Waitsfield-Fayston Telephone Company, Inc., d/b/a Waitsfield Telecom and d/b/a Champlain Valley Telecom; Northfield Telephone Company; Perkinsville Telephone Company; Ludlow Telephone Company; Franklin Telephone Company; and Vermont Telephone Company, Inc., d/b/a VTel);
- New England Cable and Telecommunications, Inc. and Comcast Phone of Vermont, LLC (collectively, "NECTA/Comcast");
- segTEL, Inc. ("segTEL");
- Sovernet, Inc. ("Sovernet");
- Vermont Electric Cooperative, Inc. ("VEC");
- City of Burlington Electric Department;
- Green Mountain Power Corporation;
- One Communications Corp. ("One Communications"); and
- Level 3 Communications, LLC ("Level 3").

On August 14, 2007, we allowed Level 3 to withdraw.[8]

C. Discovery and Testimony

The Petitioners filed direct testimony on March 23, 2007. After two rounds of discovery, the Department and intervenors filed direct testimony on May 24, 2007. After one round of discovery, the Petitioners filed rebuttal testimony on June 27, 2007. After one round of discovery, the Department and intervenors filed surrebuttal testimony on August 10, 2007.

D. Public Hearings

Public hearings were held as follows:

- On May 3, 2007, using the Vermont Interactive Television ("VIT") network sites at Bennington, Castleton, Johnson, Lyndonville, Middlebury, Montpelier, Randolph Center, Springfield, St. Albans, White River Junction and Williston;

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8. Procedural Order on Motion to Withdraw, 8/14/07.

- On June13, 2007, in Cabot, Vermont, which is within FairPoint's current service territory; and
- On August 1, 2007, using the VIT sites at Brattleboro, Rutland, Johnson and Waterbury.

E. Technical Hearings and Briefs

The Board convened technical hearings in Montpelier on the following dates:

- September 5–7 and
- September 17–21, 2007.

Direct briefs were filed on October 17, 2007. Reply briefs were filed on November 2, 2007.

F. Confidentiality

During the course of this proceeding, the Petitioners identified various information that they requested that the Board treat as confidential. The Board has previously observed the "Vermont law recognizes that some commercial information is entitled to protection that would limit its disclosure to the public or even other parties."[9] At the same time, we have consistently stated, the Board's policy is to ensure that as much information is publicly available as possible so that any orders "be transparent in our assumptions and reasoning."[10] Requests for confidentiality must be narrowly drawn to encompass only information whose disclosure would create competitive harm or reveal personal information. These requests must be accompanied by specific averments as to the reasons confidentiality is necessary. We have reminded parties here of this policy, which has resulted in a substantial amount of information that was originally claimed confidential being made public.

On March 28, 2007, we issued an Order approving a protective agreement that was executed by all of the parties. On April 27, 2007, we granted previous motions by FairPoint and Verizon for confidential treatment of certain prefiled testimony. Subsequent motions for

9. *Investigation into General Order No. 45 Notice filed by Vermont Yankee Nuclear Power Corporation*, Docket 6545, Order of 3/29/02 at 1.

10. *Petition of UPC Vermont Wind, LLC for a Certificate of Public Good*, Docket 7156, Order of 8/18/06 at 1.

confidential treatment were filed on May 23, 2007, by Verizon, and on May 24 and May 29, 2007, by FairPoint.

On June 5, 2007, we requested comments concerning the motions. On June 15, the Department responded, noting concerns about the adequacy of the averments filed by FairPoint and Verizon in support of their respective confidentiality motions. On August 10, 2007, the Department submitted a letter to the Board stating that its specific concerns regarding the Verizon averments had been addressed satisfactorily by Verizon, but continuing to express concerns about the logistical difficulties posed in this docket due to the volume of information for which Petitioners were seeking confidential treatment.

Subsequently, Verizon and FairPoint filed additional motions for confidential treatment of certain prefiled testimony.

On August 22, 2007, we issued a memorandum noting that a large portion of the testimony and exhibits in this docket has been filed under the Protective Agreement as Allegedly Confidential. In some cases, motions had been made to protect specific elements of prefiled testimony. In other cases, motions had been filed referring to underlying discovery materials, but did not list specific lines in testimony or specific exhibits attached to testimony. We instructed Verizon and FairPoint to provide a complete listing of the elements of prefiled testimony, filed by any party, to which Verizon or FairPoint wished to allege confidentiality during the technical hearings. Both Verizon and FairPoint subsequently made these filings.

At the technical hearings, all pending motions for confidential treatment were treated as granted. Portions of the technical hearings involving confidential information were conducted under seal.[11] The confidentiality of specific materials was discussed, and some confidentiality claims were later withdrawn.

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11. On September 5 and 6, 2007, sealed testimony was taken from Walter Leach, a FairPoint witness on confidential matters. During those sessions, any party that had signed the protective agreement was allowed to be present and participate, but the public was excluded. In addition, on September 6, 2007, a separate sealed session was conducted, further examining Mr. Leach regarding matters considered highly confidential; and certain parties who are also competitors of FairPoint were also excluded. *See* tr. 9/6/07 at 5–6.

G. Other Matters

On June 25, 2007, FairPoint moved to exclude on hearsay grounds certain portions of the direct testimony of Dr. Kenneth Peres, an expert witness for the Labor Intervenors. On June 29, 2007, Labor responded, arguing that the testimony at issue was admissible through certain hearsay exceptions. We took the motion under advisement on July 12, 2007, and declined to rule in advance of the technical hearings. Ultimately, FairPoint consented to the admission of Dr. Peres' direct testimony in full.

On July 12, 2007, we requested comments regarding whether the scope of this proceeding should be broadened to include 30 V.S.A. §226b or whether we should reopen Verizon's Incentive Regulation Plan for further review pursuant to 30 V.S.A. §226b(i). Having received, reviewed and considered comments from Verizon, FairPoint and the Department, we decided not to expand the scope of this proceeding and not to reopen the Incentive Regulation Plan.[12]

On September 17, 2007, the Labor Intervenors made a motion to unseal a portion of the evidentiary record. FairPoint filed a response on the next day. After oral argument, we indicated on the record that the Board would stay its ruling until the next day to give FairPoint and the Labor Intervenors a further opportunity to reach a mutually agreeable solution. On September 19, FairPoint and the Labor Intervenors reported on the record that they had been able to settle their differences. A portion of the record thereafter was removed from being under seal.

On September 28, 2008, the Eight Independents filed a notice that they had entered into a Settlement Agreement with FairPoint regarding continuation of existing arrangements between themselves and Verizon.

On October 26, 2007, FairPoint filed an information copy of a settlement agreement it had reached with Sovernet and segTEL (the "CLEC Settlement").[13] The settlement clarified FairPoint's obligations to Sovernet and segTEL under various federal laws, including sections 251 and 271 of the Federal Telecommunications Act of 1996 (the "Act"). It also obligated FairPoint to provide specified wholesale services, including wholesale DSL for three years, and it

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12. Order of 8/1/07.

13. The stipulation also included other telecommunications service providers who are not parties in this proceeding.

set caps on certain wholesale prices. The settlement also provided a detailed procedure for FairPoint to assume Verizon's wholesale obligations.

On October 25, 2007, One Communications filed a motion to reopen the record to allow additional factual information, suspend the schedule, and hold additional hearings regarding the CLEC Settlement. We denied the motion in an Order issued on November 6, 2007, but we invited other parties to comment. Several parties did file comments.

FairPoint and Verizon plan to close the transaction on January 31, 2008, and they have requested a decision from each state, including the Board, by mid-December.

On December 13, 2007, FairPoint filed a copy of a settlement between various parties in Maine. The settelement, if approved, would have the effect of changing certain elements of the Proposed Transaction. The Board asked FairPoint whether, in light of the settlement, it still requested that the Board issue an order in December. FairPoint responded that it still sought an order on the original timetable and evidentiary record.

III. Positions of the Parties

A. FairPoint

In support of its joint petition with Verizon, FairPoint argues that it has made commitments to Vermont that will: improve customer service; enhance the quality of service; extend broadband by December 31, 2010, to significantly more customers than otherwise would occur (and continue to expand broadband thereafter); and stimulate Vermont's economy through investment and increased employment. FairPoint notes that Verizon is not obligated today or in the future to match the breadth of FairPoint's explicit commitments, and FairPoint claims it is uniquely positioned to deliver the advanced communications services that Vermont customers deserve.

FairPoint argues that the principal question is not whether Verizon's customers and the state will be better off as a result of the transaction. Rather, FairPoint sees the principal issue as whether it has the technical, managerial and financial capabilities to fulfill its express commitments. FairPoint asserts that if the Board approves the transaction:

- Customers served today by Verizon will be served by a carrier that will invest to bring broadband addressability to up to 88% of Vermont's access lines by 2010;
- Vermont customers will be served by a carrier that is rated good to excellent on service quality, broadband deployment and knowledgeable personnel;
- More than 700 jobs — specifically including at least 145 in Vermont and another 50 in Littleton, New Hampshire — will be added to the northern New England region;
- FairPoint's employment and investment plans will contribute at least $100 million initially and $45 million annually thereafter to the Vermont economy;
- Customers will be served by next-generation back-office systems designed by FairPoint and its partner, Capgemini U.S. LLC ("Capgemini"), a telecommunications consulting firm that has designed state-of-the-art procurement, billing, and back-office systems for major telecommunications companies throughout the world; and
- Competitive Local Exchange Carriers ("CLECs") and other wholesale customers will receive wholesale and interconnection services from an experienced, dedicated team led by a manager who understands CLEC and wholesale customer concerns and how to address them.

FairPoint argues that it has a seasoned and well-respected management team accustomed to providing service in rural areas, and that it provides a high proportion of those customers with broadband availability.

FairPoint also contends that it can and will deliver on its commitments, and that the record demonstrates the necessary capabilities to meet its obligations. FairPoint reports that it has successfully acquired more than thirty local-exchange carriers since 1993. It also claims that the financial community has responded positively to the transaction's structure, to FairPoint's selection of Capgemini, to the specific terms negotiated with Verizon, and to FairPoint's ability to rely on its knowledge and experience from past acquisitions.

On financial issues, FairPoint argues that free cash flow is the most relevant measure of a company's health and that FairPoint projects that it will generate over $200 million in annual free cash flow over the first five years following the closing and only slightly lower amounts thereafter. FairPoint contends that its projections are conservative for the rural local exchange carrier industry. In addition, FairPoint argues that it has limited its exposure to fluctuations in the financial markets and, thereby, its cost of debt through the use of interest-rate swap agreements. Finally, FairPoint reports that it is prepared to reduce or not pay dividends on its common stock if necessary to ensure the financial stability of the transferred Verizon operations and the fulfillment of its commitments. In conclusion, FairPoint argues that Vermont customers and the state will be served by a company that wants to be here, that is focused on delivering quality advanced communication services to northern New England, and that is committed to investment in and service to rural states like Vermont.

B. Verizon

Verizon also argues that the transaction would promote the public good and should be approved. Verizon contends that FairPoint is experienced at offering high-quality services in rural and small urban areas and is dedicated to such markets. Verizon asserts that FairPoint has the financial resources and business plan to operate a new Vermont business in an efficient and fiscally responsible manner.

Verizon also contends that the transaction would be beneficial to Verizon's existing employees and the Vermont economy, in part because of continued employment available for current Verizon employees and in part due to newly created jobs. Verizon also points to FairPoint's investment plans for broadband expansion in Vermont, which it states should provide a platform that can be upgraded to provide additional services, including Internet Protocol Television ("IPTV"), in the future.

Verizon also asserts that the transaction will be "seamless" to Vermont customers[14] who will continue to receive the same services and rates. Verizon notes that FairPoint will remain subject to the same service quality obligations that today apply to Verizon, as well as the obligations of Verizon under the 2005–2010 Amended Vermont Incentive Regulation Plan (the "Incentive Regulation Plan"). As to wholesale service, Verizon notes that FairPoint would honor existing wholesale arrangements, including contracts and tariffs.

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14. Verizon Brief at 3.

C. Department of Public Service

The Department asserts that Verizon is today providing "substandard service and inconsistent broadband access" and that Verizon "chooses not to serve the public good of Vermont as it should, and as it could."[15] The Department contrasts this with FairPoint, which it characterizes as desiring to provide good service, but which also presents substantial risks about whether it "can deliver."[16] The DPS asks, assuming Verizon will leave Vermont, whether a way can be found to reduce those risks to an acceptable level.

Because of its inherent risks, the Department argues that the transaction, as it is currently defined by the Petitioners, does not promote the general good.[17] Nevertheless, the Department asserts that the transaction would serve the public good if FairPoint can convert its stated good intentions into "tangible reality."[18] To accomplish this, the Department recommends imposition of 56 conditions. These conditions relate to finances, service-quality and customer-service, systems-conversion, service to competitors, and pricing and service-availability commitments. Notable among these is a recommendation that FairPoint provide "consistent coverage" of broadband, which it defines as providing broadband service to 100 percent of the lines in at least 50 percent of its exchanges by the end of 2010. Also, the Department recommends requiring FairPoint establish a separate legal entity within Vermont to separate all Vermont related assets and liabilities, if any, from the assets and liabilities of other FairPoint companies. Only if all conditions are imposed and accepted, the Department concludes would "the transaction risk become — more manageable,"[19] and only then would the public good be served.[20]

D. Labor Intervenors

Labor Intervenors contend that the proposed transaction does not promote the public good and should be rejected because FairPoint is not financially stable and sound. The Labor

15. DPS Brief at 105.
16. DPS Brief at 105.
17. DPS Brief at 1.
18. DPS Brief at 1.
19. DPS Brief at 106.
20. DPS Brief at 1.

Intervenors characterize FairPoint's financial assumptions as "wildly optimistic,"[21] and they maintain that actual financial weakness is likely to severely constrain FairPoint's ability to provide safe and reliable service. Like the Department, Labor recognizes that Verizon has "presented challenges to regulators," but they contend that if the proposed transaction is approved, "it can get worse for Vermont, conceivably much worse."[22] Labor argues that no set of conditions can be drafted to cure these fundamental problems with the transaction.[23]

Nevertheless, if the Board should decide to approve the transaction, Labor recommends three groups of significant conditions. First, Labor recommends that the amount of cash paid by FairPoint be effectively reduced by ordering Verizon to bring its own network "up to standards" in several respects before departing from Vermont.[24] Second, Labor recommends restricting in several ways FairPoint's ability to transfer cash from its Northern New England operation ("NNE") to the parent, some of these restrictions are triggered by failure to meet service quality standards. Notably, Labor recommends conditions that would limit dividends from the newly-acquired territories to FairPoint until a sufficient reserve is established for capital expenses. Third, Labor recommends numerous service quality conditions aimed at reducing the risk that service quality penalties might become a routine cost of business.

E. Other Parties

NECTA/Comcast intervened in this proceeding to ensure that any merger would include conditions that avoid or mitigate obstructions and impairments of competition, and that mitigate against material risks to competition arising out of the proposed transaction. NECTA/Comcast argues that the petitioners have not met their burden of proving that their proposed merger transaction would promote the public good and would obstruct and impair competition within Vermont.[25] Primarily, NECTA/Comcast argue that FairPoint has not demonstrated the ability to perform Verizon's wholesale service obligations and that FairPoint has sought to evade some of

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21. Labor Brief at 46.
22. Labor Brief at 48.
23. Labor Brief at 54.
24. Labor Brief at 51.
25. NECTA/Comcast Brief at 8, 9.

Verizon's existing obligations to other carriers or to degrade existing levels of wholesale service.[26] If the Board does approve the transaction, NECTA/Comcast suggests that the Board should also impose 13 conditions. These include prohibiting FairPoint from seeking relief under certain federal statutes that apply to smaller incumbent telephone companies, requiring extensions of existing interconnection agreements and pole attachment rates, mandating an internal FairPoint organization to serve wholesale customers, and reimbursing wholesale customers for the costs of adapting to FairPoint's new systems.

Sovernet and SegTEL are wholesale competitors who originally urged rejection of the merger on the ground that it would obstruct or prevent competition in the wireline telecommunications market.[27] On October 26, 2007, FairPoint filed its stipulation with these companies ("CLEC Stipulation").[28] In their reply brief, Sovernet and segTEL then supported the merger, but only so long as the Board's final order either approves the settlement or incorporates the terms of the settlement conditions.[29]

One Communications urges the Board to deny the petition. It argues that the transaction has not been shown to promote the public good because FairPoint is not financially sound, FairPoint lacks the technical knowledge and business reputation to provide quality wholesale services, and the transaction will not produce efficiencies to benefit customers. One Communications further argues that, absent conditions, the merger will impair and obstruct wholesale competition. One Communications also filed comments on the CLEC Stipulation, arguing that it provides only incomplete protection to competitive local exchange carriers who were not signatories to the stipulation. One Communications concludes that if the Board decides to approve the transaction proposed by FairPoint, the Board should require that certain provisions of the CLEC Settlement be applicable to all CLECs in Vermont. On selected issues, One

26. NECTA/Comcast Brief at 8-9.

27. Sovernet/segTEL Brief at 1.

28. The stipulation also included other telecommunications service providers who are not parties in this proceeding.

29. Sovernet/segTEL Reply Brief at 1.

Communications also recommends more stringent conditions than those contained in the CLEC Settlement.[30]

The Eight Independents were interested in only some wholesale issues in this proceeding, and they participated briefly in technical hearings. They reached a settlement with FairPoint regarding the continuation of the arrangements that now exist between Verizon and each of the Eight Independents regarding the joint management of the public switched telephone network in the state. The Eight Independents now request a finding in the Board's Order stating that their agreement with FairPoint will ensure that the merger will not cause any material change to any rate, term or condition of the services currently in place between Verizon and the Eight Independents.[31]

VEC was originally concerned about how FairPoint would maintain joint facilities, including poles, in VEC's territory. VEC and FairPoint filed a Memorandum of Understanding on September 19, 2007, that resolves the parties' disputes. VEC now supports approval, provided the orders and findings of the Board are consistent with the MOU.

The City of Burlington Electric Department and Green Mountain Power Corporation were admitted as parties, but they did not participate and did not file briefs.

IV. Legal Standard

A. Standard of Review

1. Review of the Transaction

Before the transactions contemplated by the Merger Agreement may be executed, approval from this Board is required under 30 V.S.A. §§ 107, 109, 311 and 231. Section 107 requires advance approval for acquisition of a "controlling interest in any company subject to the jurisdiction of the public service board." Section 109 requires prior approval of a substantial sale or lease of a utility's corporate property.[32] Section 311 applies to mergers.[33] The general

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30. One Communications Comments of November 14, 2007, at 2.

31. Letter from Paul Phillips to Susan Hudson, dated Sept. 28, 2007, at 2.

32. Relevant portions of the statute apply whenever a utility would "make a sale or lease or series of sales or leases in any one calendar year constituting ten percent or more of the company's property located within this state and actually used in or required for public service operations nor merge nor consolidate pursuant to the provisions of (continued...)

standard for applying these statutes is whether the transaction would promote the public good of the state.[34] The Board has previously stated that fifteen criteria are used to examine change of control transactions under 30 V.S.A. §107. These are:

1. Legal authority for the transaction from the Federal Communications Commission;
2. Availability of emergency services;
3. Compatibility with neighboring systems;
4. Just and reasonable terms and conditions of service;
5. Service quality;
6. Customer Service;
7. Quality of the facilities;
8. Rate of capital investment;
9. Financial stability and soundness;
10. Control of affiliate interests;
11. Competence of management;
12. Technical knowledge, experience and ability;
13. Business reputation;
14. Transaction should produce efficiencies; and
15. Transition should not impair competition.[35]

The Board has also held that not all fifteen criteria are of equal importance, and the five criteria regarding the surviving entity are of primary interest (Criteria Nos. 9, 12, 13, 14, and 15).[36] The Board concluded that "[w]hile each of the fifteen items may be considered in

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32. (...continued)
sections 301–307 of this title, nor after any such sale, lease, consolidation or merger shall any subsequent like action be taken." 30 V.S.A. § 109.

33. Section 311 requires that a consolidation or merger of a regulated utility "shall not become effective" without the approval of the public service board after due notice.

34. *See* 30 V.S.A. §§ 107(b), (c)(4)("promote the public good"); 109 ("promote the general good of the state").

35. *Joint Petition of New England Telephone & Telegraph Company, d/b/a NYNEX, NYNEX Corporation, and Bell Atlantic Corporation for approval of a merger of a wholly-owned subsidiary of Bell Atlantic Corporation into NYNEX Corporation*, Docket 5900, Order dated 2/26/97 at 8–9.

36. *Joint Petition of Bell Atlantic Corp. and GTE Corp. for approval of Agreement and Plan of Merger*, Docket 6150, Order of 9/13/99 at 48-49.

reaching a decision, that decision, finally, consists of determining whether, based on the record, and balancing all of the factors, the public good standard is satisfied."[37]

The Board has previously determined that these same standards apply for reviews under section 109.[38] Also, under section 311, the Board must find that the transactions will not "result in obstructing or preventing competition in the purchase or sale" of a regulated "product, service or commodity."[39] The Board has previously determined that the fifteenth criterion of the section 107 review also addresses the standard under section 311.[40]

In reviewing acquisitions, the Board has typically grouped the preceding 15 requirements into five principal areas. These are:

1. Whether the surviving company is technically competent;
2. Whether the surviving company is financially sound;
3. Whether the surviving company will act as a fair partner in business transactions with the citizens of Vermont;
4. Whether the surviving company will create efficiencies that will benefit customers; and
5. Whether the transaction will cause impairment of or obstruct competition.[41]

The Board has also made clear that its analysis of both the five considerations noted above, as well as the 15 specific factors, is directed fundamentally towards meeting the requirements that an acquisition must promote the public good.[42]

<u>2. Issuance of Certificate of Public Good</u>

30 V.S.A. § 231 requires a person desiring to "own or operate a business over which the [Board] has jurisdiction" to obtain a Certificate of Public Good ("CPG"). In determining whether

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37. Docket 6150, Order of 9/13/99 at 48.

38. Docket 5900, Order of 2/26/97 at p.1 n.2.

39. *See* 30 V.S.A. § 311.

40. Docket 5900, Order of 2/26/97 at 20.

41. *Joint Petition of Green Mountain Power Corporation, Northern New England Energy Corporation and Northstar's Merger Subsidiary Corporation*, Docket 7213, Order of 3/26/07 at 9–10; *Joint Petition of Verizon Communications, Inc. and MCI, Inc. for approval of an Agreement and Plan of Merger resulting in MCI becoming a wholly-owned subsidiary of Verizon*, Docket 7056, Order of 11/29/05 at 7; Docket 6150, Order of 9/13/99 at 48–49.

42. Docket 7213, Order of 3/26/07 at 10.

to issue a CPG, the Board must find that it will promote the general good of the State of Vermont.[43] The established criteria to determine whether an entity should be granted a CPG are consistent with the Board's examination of merger and acquisition transactions. These are:

(1) technical expertise;
(2) adequate service;
(3) facility maintenance;
(4) balance between customers and shareholders;
(5) financial stability;
(6) company's ability to obtain financing;
(7) business reputation; and
(8) relationship with customers.

These criteria are guidelines only, and the Board may deviate from them as the circumstances require. Indeed, the Board's authority under section 231 is broad. Because 30 V.S.A. § 203 permits the Board to exercise its jurisdiction "so far as may be necessary to enable [it] to perform [its] duties and exercise the powers conferred upon [it] by law," in issuing a CPG, the Board may tailor conditions appropriate to the planned activities of the petitioner.[44]

3. ETC Designation

In order for a telecommunications carrier to be eligible for federal universal support, it must be designated as an Eligible Telecommunications Carrier ("ETC"). [45] Under federal law, the Board is responsible for designating ETCs in Vermont, based upon standards established by federal law.[46]

Federal law establishes three fundamental requirements for receiving ETC designation. First, the carrier must offer the services that are supported by the federal "universal service

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43. *Petition of USGen New England, Inc., for authority to transfer its hydroelectric facilities located in Vermont to TransCanada Hydro Northeast, Inc.*, Docket 7038, Order of 3/25/05 at 9–10.

44. *See Petition of New England Power Company*, Docket 6039, Order of 6/29/98, at 15-17; Docket 7038, Order of 3/25/05 at 9.

45. See 47 U.S.C. § 214(e); 47 C.F.R. § 54.201.

46. *See* 47 C.F.R. §§ 54.101, et seq.

support" mechanism. Those nine services consist of the following: voice-grade access to the public switched network; local usage; dual-tone, multi-frequency signaling or its functional equivalent; single-party service or its functional equivalent; access to emergency services; access to operator services; access to interexchange service; access to directory assistance; and toll limitation for qualifying low-income consumers.[47] Second, the carrier must offer these nine services throughout the service area for which the designation is received, and the services must be offered either using the carrier's own facilities or a combination of its own facilities and resale of another carrier's services.[48] Finally, the carrier must advertise the availability of those services using media of general distribution.[49]

4. Incentive Regulation Plan

FairPoint seeks to adopt and abide by the terms of Verizon's existing Incentive Regulation Plan. Verizon's existing Incentive Regulation Plan was reviewed and authorized pursuant to 30 V.S.A. § 226b, which contains numerous criteria. Section 226b does not expressly contain a standard governing the transfer of an alternative regulation plan.

All parties agree that the criteria used in reviews under Section 107 are sufficient to determine the additional question of whether FairPoint should be allowed to adopt Verizon's Incentive Regulation Plan. These criteria are substantially the same as the § 226b(c) standards. Accordingly, it is not necessary to set a general standard for transfer of a alternative regulation plan from a selling utility to a purchasing utility. We will, however, consider the proposed Incentive Regulation Plan transfer as one factor, among many, in determining whether the proposed transaction will promote the public good.

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47. *See* 47 C.F.R. § 54.201.
48. *See* 47 C.F.R. § 54.201(d)(1).
49. *See* 47 C.F.R. § 54.201(d)(2).

5. Applicable Standard

Based on the preceding discussion, we apply the following standard in determining in this proceeding whether the proposed transaction promotes the public good of the state. FairPoint carries the burden of proof on all of the following questions:

1. Whether the new company is competent. This includes examining whether:
    a. the new company's management is competent;
    b. the new company is technically competent;
    c. the new company has a good business reputation; and
    d. the new company has obtained all necessary regulatory approvals.
2. Whether the new company is financially sound.
3. Whether the new company will act as a fair partner in business transactions with the citizens of Vermont. This includes examining whether:
    a. terms and conditions of service will be fair and reasonable;
    b. service quality will be adequate;
    c. customer services will be adequate;
    d. emergency services will be adequate; and
    e. investment will be adequate.
4. Whether the new company will create new benefits for the state. This includes examining whether the proposal will:
    a. provide a better, stronger, more capable or more ubiquitous network;
    b. produce efficiencies in operation; and
    c. provide economic benefits to the state economy or other benefits.
5. Whether the transition from the old company to the new company will be adequately managed.
6. Whether the transaction will impair or obstruct competition.

V. FINDINGS AND DISCUSSION

A. The Proposed Transaction

1. Findings

a. Verizon

1. Verizon (together with certain affiliates) is a New York corporation that provides regulated telecommunications services in Vermont (including local exchange service and exchange access service) to approximately 360,000 access line equivalents in the state. Exh. DPS Cross-19 at 24, 173.

2. Verizon is an indirect, wholly-owned subsidiary of Verizon Communications Inc. Exh. DPS Cross-19 at F-75.

3. NYNEX Long Distance, VSSI and GTE.net LLC ("GTE.net") are indirect, wholly-owned subsidiaries, and BACI is a direct, wholly-owned subsidiary of Verizon Corporation. NYNEX Long Distance, BACI and VSSI provide interexchange services in Vermont. Exh. DPS Cross-19 at F-75.

4. Verizon's operation in Vermont predates the requirement of a CPG under 30 V.S.A. § 231(a). NYNEX Long Distance, BACI, and VSSI have been granted CPGs under 30 V.S.A. § 231 to conduct businesses subject to the Board's jurisdiction and will retain those CPGs. Smith pf. at 21.

b. FairPoint

5. FairPoint is a publicly-traded telecommunications company, incorporated in Delaware. Joint Petition at 3.

6. FairPoint provides, through its local exchange carrier operating subsidiaries, (1) wireline local exchange and exchange access service to approximately 310,000 access line equivalents and (2) domestic and international long-distance toll services in 18 states, including Vermont, New Hampshire and Maine. Exh. DPS Cross-17 at 11, 173, F-22.

7. A subsidiary of FairPoint, FairPoint Vermont, Inc., d/b/a FairPoint Communications (hereinafter "FairPoint Vermont"), presently has a CPG and provides intrastate telecommunications service in Vermont. Skrivan reb. pf. at 12.

c. Merger Agreement

8. On January 15, 2007, Verizon, FairPoint, and Northern New England Spinco Inc. ("Spinco") entered into an Agreement and Plan of Merger (the "Merger Agreement") and Distribution Agreement under which Verizon would transfer its local and long distance businesses in Vermont to FairPoint, as part of a broader transaction in which FairPoint will acquire all of Verizon's local and local long distance businesses in Maine, New Hampshire and Vermont.[50] Smith pf. at 3.

9. Under the Proposed Transaction, Verizon would transfer its local exchange, long distance, exchange access, and related business activities in Maine, New Hampshire and Vermont to a new entity, Spinco, and then spin-off the stock of Spinco to Verizon Communications' shareholders. Spinco would then be immediately merged into FairPoint. Specifically, the transaction will be accomplished through the following steps:

> a. Verizon New England transfers its assets, liabilities and customer relationships relating to its local exchange, intrastate toll and exchange access operations in Vermont, New Hampshire and Maine to Telco, a wholly-owned subsidiary of Verizon New England;
>
> b. NYNEX Long Distance, BACI, and VSSI transfer their accounts receivable, liabilities and customer relationships relating to their long-distance and certain non-regulated operations in Maine, New Hampshire and Vermont to Enhanced Communications of Newco, a wholly-owned subsidiary of Spinco, through a series of intermediate transfers;[51]
>
> c. Verizon New England transfers the stock in Telco to Spinco, through a series of intermediate transfers;
>
> d. Verizon Communications distributes the stock of Spinco directly to Verizon's shareholders;
>
> e. Spinco is merged into and with FairPoint, with FairPoint as the surviving company.

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50. The northern New England properties being transferred under the Proposed Transaction are referred to herein as "NNE."

51. Certain other Verizon affiliates, which are not subject to Board regulation, will also transfer certain assets, liabilities and customer relationships to Newco. Smith pf. at 7. Depending on the tax consequences, Verizon may elect to create Spinco as a direct subsidiary of Verizon New England, rather than Verizon Communications. Smith pf. at 13. As of the date of hearing, Verizon had not yet received the Internal Revenue Service ruling that Verizon needs to help determine which structure to employ. Tr. 9/7/07 (Smith) at 49–50, 81–82.

Smith pf. at 4, 7, 10; exhs. Verizon-SES-1, SES-2.

10. The spin-off and the merger are designed to be tax-free to Verizon and its shareowners under the Internal Revenue Code. Smith pf. at 3, 17; Nixon pf. at 9.

11. Following notification and the ability to opt-out, current customers of Verizon will become customers of Telco, and current customers of NYNEX Long Distance, BACI and VSSI will become customers of Newco. Exh. Verizon-SES-1, Section 7.6(f); Smith pf. at 4, 8.

12. The business to be operated by Newco includes the following:

> (a) consumer and small business switched and certain dedicated long distance service to customers located in the NNE territory;
>
> (b) large business switched and dedicated long distance service currently offered by VZ Select Services Inc. ("VSSI") to customers located in the NNE territory;
>
> (c) the delivery of dial-up, DSL and fiber to the premises (a/k/a FiOS) data and dedicated internet access services to customers located in the NNE territory;
>
> (d) customer premise equipment sales, and installation and maintenance services currently offered by VSSI to customers located in the NNE territory; and
>
> (e) private line service to current customers of VSSI where the line originates and terminates in the NNE territory.

Smith pf. at 6–7.

13. With respect to Verizon's wholesale obligations, Verizon will assign to FairPoint contracts, including interconnection agreements and commercial agreements, addressing areas completely within Maine, New Hampshire and Vermont. Contracts addressing areas totally outside of the three states will be unaffected. Verizon will offer to amend the contracts addressing areas both within and outside of the three states, to exclude service within the three states and FairPoint will offer to negotiate replacement contracts on substantially the same terms. Verizon and FairPoint will renegotiate and amend volume commitments to reflect the change in scope of service post-closing. Smith pf. at 21–22.

14. Upon closing, NYNEX Long Distance and BACI will cease doing any business subject to the Board's jurisdiction, except that NYNEX Long Distance and BACI will continue to

terminate long distance traffic in the three states and VSSI will continue to offer prepaid card, payphone dial-around services and dedicated internet access. Smith pf. at 21.

15. Businesses conducted by Verizon Business Global LLC (successor to the business of MCI, Inc.), Cellco Partnership (d/b/a Verizon Wireless), Verizon Network Integration Corp. (network integration services), Verizon Federal Inc. (customized communications services), Verizon Federal Network Systems LLC (enterprise-wide communication solutions), and Verizon Global Networks Inc. (long distance Verizon network maintenance) will not be transferred. Smith pf. at 11, 20–21.

16. As a result of the Proposed Transaction, the number of access lines served by FairPoint will increase by nearly 500 percent. After closing, FairPoint will have an estimated 1,790,974 access lines. This will include 317,645 Vermont lines acquired from Verizon, more than one line in six. It will also include 311,150 lines in legacy FairPoint companies in the 18 states in which it offers service. Wheaton pf. at 28.

17. FairPoint Vermont served 5,706 access lines in 2006. Vermont Department of Public Service, *Utility Facts*, (updated Aug., 2007) at 32.[52]

18. As of the closing, FairPoint will be owned by the shareholders of Verizon Communications and FairPoint in an approximately 60%/40% ratio, and FairPoint will directly own Telco and Newco. In addition, FairPoint will own other subsidiaries that pre-existed the merger transaction. Smith pf. at 4, 19; Nixon pf. at 9–10.

19. FairPoint plans to keep its existing operating companies separate from the newly-acquired properties, at least initially. FairPoint plans to integrate FairPoint Vermont into the newly acquired operations within two or three years. Nixon pf. at 10; tr. 9/20/07 at 239–242 (Nixon).

20. The total value to be received by Verizon and its stockholders in this transaction will be approximately $2.715 billion. Leach pf. at 15.

21. FairPoint is obligated to pay Verizon $1.7 billion for the transferred business, consisting of a special dividend to Verizon equal to the tax basis of Verizon's investment in Spinco

52. Utility Facts is available at: http://publicservice.vermont.gov/pub/other/utilityfacts2006.pdf. This finding is based on administrative notice. Parties may file any exceptions in motions to reconsider.

(expected to be roughly $900 million) and the remainder in the form of senior, unsecured ten-year notes. Smith pf. at 14–15.

22. The expected $800 million in debt to Verizon will be incurred by Spinco. Following the merger with FairPoint, these will become obligations of FairPoint. Smith pf. at 14–15, 17.

23. FairPoint has secured $2.08 billion in debt commitments. This includes the debt to Verizon, $1.1 billion through other variable rate bank loans, and $0.2 billion through a revolving loan. Smith pf. at 13; tr. 9/5/07 at 78 (Leach); tr. at 9/6/07 at 92–94 (Leach).

24. Following the closing, FairPoint will have approximately $2.35 billion in debt and have access to another $400 million in debt. Smith pf. at 15.

d. Employees

25. Under an Employee Matters Agreement, employees that Verizon determines not to retain and whose primary duties relate to the transferred business will continue their employment with Telco and Newco after the closing. Exh. Verizon-SES-3, Section 4.1.

26. FairPoint will honor the commitments to the approximately 3,000 current Verizon employees who will be transferred. The collective bargaining agreements with the IBEW and the CWA will continue and management employees will receive the same levels of compensation and benefits. Leach pf. at 8–9; Nixon pf. at 16–17.

27. The employees who will continue with FairPoint following the merger will continue in their same or similar functions and same locations. Nixon pf. at 16.

28. FairPoint will be responsible for all post-retirement obligations associated with persons employed by Telco and Newco as of the closing. Verizon will transfer assets from its pension plans in an amount that fully funds a newly-established FairPoint pension plan at closing. The FairPoint plan will provide the same retirement benefits as those currently provided by Verizon. Smith pf. at 18; exh. Verizon-SES-3, Section 5.2; Nixon pf. at 16.

29. FairPoint will not be responsible for post-retirement obligations with respect to current Verizon retirees and any Verizon employees who retire prior to closing. Smith pf. at 12; exh. Verizon-SES-3, Section 5.2.

30. Under the Employee Matters Agreement, during the first year after closing, a Verizon employee who voluntarily leaves may not be hired by Verizon until six months after the employee's departure. Tr. 9/7/07 (Smith) at 29; exh. Verizon-SES-3, Section 4.3(a).

B. FairPoint's technical competence

1. Management competence

a. Findings

31. Eugene B. Johnson is FairPoint's Chairman and CEO. He will be the Chairman and CEO of the merged company, and it is expected that Mr. Johnson will continue to serve at least until the end of 2009. He has more than twenty years of experience in the telecommunications industry. Leach pf. at 17; exh. DPS Cross 19 at 41, 189.

32. Peter Nixon is FairPoint's President and has been designated to serve as the full-time chief executive for the newly-acquired properties. He is recognized to have substantial operating experience in the telecommunications industry, with FairPoint and with rural local exchange carriers. He has been employed in the telecommunications business since 1978. At FairPoint he has served as Chief Operating Officer, President of the Eastern Region, President of the Telecom Group, and Senior Vice President – Corporate Development. Nixon pf. at 1; Wheaton pf. at 24.

33. Although Mr. Nixon is the President of FairPoint, his direct responsibility will be limited to the acquisition properties here. Lisa Hood, Chief Operating Officer of FairPoint, will remain responsible for FairPoint Vermont Telephone, the existing FairPoint property in Vermont. Tr. 9/20/07 at 98, 101 (Nixon).

34. Walter E. Leach, Jr. is FairPoint's Executive Vice President for Corporate Development. He has extensive experience in the utility business, having been with FairPoint for 13 years and with an independent power company for 10 years before joining FairPoint. He also served as the Vice President of Investor Relations for the Pillsbury Company, also a publicly-traded company. Tr. 9/5/07 at 45 (Leach).

35. The financial community believes that FairPoint' senior management has a proven track record in acquiring properties and operating them effectively. It also believes that FairPoint has the financial acumen, discipline, experience and ability to acquire the Verizon New England

properties and to operate them effectively. Wheaton pf. at 24–25; Lafferty pf. at 28; tr. 9/21/07 at 114–115 (Wheaton).

36. The investment community also believes that Verizon will provide the necessary assistance and cooperation to FairPoint since it is important to Verizon that this sale and the system conversion be successfully completed. Wheaton pf. at 26.

37. FairPoint has defined a top-level organization chart for the Verizon New England properties. The organization plan is typical of the telecommunications industry. It reflects FairPoint's experience in providing services to rural communities, although in the future FairPoint may be subject to greater regulatory scrutiny as the prime provider of telecommunications services in each of the three New England states. Wheaton pf. at 24–26.

38. FairPoint is in the process of establishing a New England-specific senior management team focused on the three States. This will help ensure service quality and delivery. FairPoint has a knowledgeable management staff that understands both the legacy technology utilized today in the Verizon network and the "next generation" technology they plan to deploy. This knowledge was acquired on a much smaller scale than the network size associated with this acquisition. Wierson pf. at 3, 12.

39. FairPoint has filled the senior management positions of Vice President Business and Wholesale Services, Vice President Consumer and Small Business Sales and Service, Vice President Information Services/Information Technology, and Vice President Human Resources with experienced and accomplished individuals. FairPoint has filled many of these senior-level positions with seasoned individuals who have significant experience in the telecommunications industry. Several senior managers have significant experience with unionized labor relations. Nixon reb. pf. at 11, 22; *see* Lippold reb. pf. at 1.

40. FairPoint plans to hire additional management personnel prior to closing, and will also benefit from a number of senior Verizon employees who will continue with FairPoint at closing. Nixon reb. pf. at 11.

41. Following the transaction, FairPoint will locate some senior-level employees in the three Northern New England states. This will include many of FairPoint's Vice President-level leaders. Nixon pf. at 13; Nixon reb. pf. at 4, 10, 11; tr. 9/20/07 at 103–104 (Nixon).

42. FairPoint will maintain Vermont-based employees responsible for state regulatory affairs, field marketing, customer service, business account executives, and a Vermont-based sales force. Nixon reb. pf. at 20.

43. The three-state regional team will be accountable for the operational performance, financial results and customer satisfaction within northern New England and, as such, will be given the appropriate levels of authority to meet their commitments. Nixon reb. pf. at 12.

44. FairPoint intends, to the extent possible, to make decisions locally, taking into consideration the needs of customers, employees, and the Vermont, Maine and New Hampshire operations. Nixon reb. pf. at 12.

45. FairPoint, through its Board of Directors, nominates individuals for consideration as Directors and it is FairPoint's shareholders that elect the directors; the company cannot appoint Directors and/or control their election. Leach reb. pf. at 61; tr. 9/5/07 at 26–27.

46. Pursuant to the transaction documents, Verizon is entitled to 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. Leach pf. at 17; tr. 9/5/07 at 25–26 (Leach).

47. Pursuant to the transaction documents, FairPoint will designate a minimum of three of the nine initial Directors of FairPoint post-closing, and FairPoint's current Chairman of the Board, Gene Johnson, will be nominated to continue in that position for the combined company. Leach pf. at 17.

48. Although election of individuals to the Board of Directors is controlled by FairPoint's shareholders, and although FairPoint's Directors represent the entire company, FairPoint has committed to make "every effort to identify qualified Vermonters to nominate as Directors." However, FairPoint cannot control such appointments. Leach reb. pf. at 61; tr. 9/5/07 at 25–27 (Leach).

49. Verizon has nominated as director Ms. Bonnie Newman, a person with close ties to New Hampshire. Ms. Newman is a past Dean of the University of New Hampshire business school and has extensive experience on corporate boards including as former director of the Public

Service Company of New Hampshire, but she has no experience in Vermont. Tr. 9/7/07 at 63 (Smith); Leach reb. pf. at 61–62; tr. 9/5/07 at 24–26.

50. It is common practice in the utilities industry to have Boards of Directors whose membership reflects the geographical mix of its customer base. Wheaton pf. at 28.

51. FairPoint's corporate charter prohibits FairPoint from agreeing that its Board of Directors will always contain a Vermont resident. Leach reb. pf. at 61.

b. Discussion

FairPoint's management team is competent, well-respected and qualified to run Verizon's northern New England operations. FairPoint's senior management is experienced and is qualified to manage the combined and much larger company. Recently-hired managers are also well qualified and well informed. Additional staff must still be hired, but we are satisfied that the upper management of the company is well-qualified and appropriately dedicated to making this acquisition successful.

Although FairPoint's President for New England will not reside in the three states, we view it as positive that FairPoint intends to require many of its other senior-level personnel to reside in the three states, and also that FairPoint intends to give them significant decision-making authority. We also view it as positive that FairPoint will be employing many experienced Verizon employees. At closing, therefore, we anticipate that FairPoint will have a competent and well-qualified group of managers to run the combined operations.

We decline to adopt the Department's recommendation to require one of the FairPoint directors to reside in Vermont.[53] We are encouraged that FairPoint has already appointed one director from New Hampshire and expect that FairPoint will give serious consideration to appointing a director with connections to Vermont, particularly as it now makes up approximately one-sixth of FairPoint. However, a director's residency in a particular state should not be a regulatory requirement. FairPoint wishes to maintain its board as accountable to the entire corporation, not merely to one geographic interest group. We conclude that this is a reasonable organizational premise and one that is consistent with high performance for Vermont

53. Our decision makes it unnecessary to consider issues raised by FairPoint about whether the law of Delaware, FairPoint's state of incorporation, tolerates rules requiring directors to reside in particular locations.

customers. To impose a proportional representation requirement for a board of directors could also produce more new conflicts than benefits. We prefer not to enter this area at all and to judge FairPoint based on its performance.

The Department's proposed condition number 40 recommended that FairPoint should appoint a senior level person located in Vermont with responsibility for communicating with the Board and Department. We agree with this recommendation. Particularly for the first few years after closing, FairPoint will face a very significant management challenge in forming a team that can effectively oversee the very large system conversion and run the company. It is important that the company and Vermont regulators maintain a close working relationship during this period. Having a senior level person in Vermont as the principal point of contact between FairPoint and regulators should make that transition smoother.

We have been disappointed that Verizon has narrowly defined the responsibilities and functions assigned to it's current Vermont senior representative. Although that person reportedly holds a senior level position, she has no operational responsibility and is not routinely aware of installation and maintenance issues until they are brought to her attention by regulators, legislators, or other members of the public.[54] We would expect that the new senior-level person for FairPoint would have duties and knowledge that go beyond that of a government relations representative assigned to deal with regulatory "hot spots." The new FairPoint person should either have broad operational responsibility in Vermont or, at minimum, regular comprehensive interactions with the people who do have that responsibility.

Therefore we would impose the following condition if this merger were approved:

> **FairPoint shall appoint a senior level person with responsibility for communicating with the Board and Department. The person's primary place of business shall be in Vermont. The person shall**

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54. *See* tr. 9/17/07 at 1420 (Verizon representative in Vermont does not deal with daily operations); tr. 9/17/07 at 1145 (Verizon representative in Vermont not directly responsible for operations); tr. 9/17/07 at 120 (Verizon representative in Vermont addressed primarily problems brought to her attention by Department of Public Service or by legislators and did not have routine interactions with installation and maintenance personnel); tr. 9/17/07 at 117-119 (Verizon representative in Vermont did not generally know how many Verizon Vermont employees are working in Massachusetts or Rhode Island or how many employees from Massachusetts or Rhode Island are working in Vermont and Verizon Director of Operations resides in New Hampshire); tr. 9/17/07 at 134-138 (Verizon representative in Vermont did not know what percentage of large business customers in Vermont are serviced by the network formerly owned by MCI).

either have significant responsibility for Vermont operations or a regular working and reporting relationship with FairPoint managers who do have that responsibility.

2. Technical knowledge, experience and ability to provide the intended services

a. Findings

52. FairPoint is an experienced operator that knows the telecommunications business, knows what it takes to run the business and knows how to put the right people in place to run the business. Tr. 9/7/07 at 68 (Smith).

53. FairPoint was founded in 1991 to acquire and operate rural and small urban telecommunications companies, with its first acquisition in 1993. It operates 30 local exchange companies in 18 states. Nixon pf. at 5; tr. 9/19/07 at 213 (Nixon).

54. FairPoint has spent the past 15 years acquiring, integrating, and improving the networks of telephone companies. Harrington pf. at 6.

55. Currently, FairPoint serves over 300,000 access line equivalents as an incumbent local exchange carrier, including voice and Digital Subscriber Line ("DSL"). FairPoint serves approximately 64,000 access line equivalents in Vermont, Maine and New Hampshire. Nixon pf. at 5.

56. As the owner of several existing incumbent local exchange carriers and two CLEC subsidiaries, FairPoint has operated centralized systems and understands the processes used by telephone companies. Haga pf. at 3.

57. FairPoint has carried out many operating company acquisitions in the past and, therefore, is familiar with issues involved with integrating different operations. Haga pf. at 4.

58. FairPoint has offered broadband to 88 percent of its customers nationally, and to over 92 percent in the company's existing New England service territories, including lower density areas. This is superior to the 62 percent overall broadband availability in Verizon's northern New England territory, although there are important differences between FairPoint's existing service areas, which are classified by the FCC as "rural," and the current Verizon territory. Nixon pf. at 7; Harrington pf. at 10; Sicker reb. pf. at 25.

59. FairPoint has used a mix of technologies to deploy broadband, and it tailors technology choices to suit the demands and conditions of each geographic area. Sicker reb. pf. at 24.

60. FairPoint has made a significant commitment to the success of the integration by dedicating Mr. Nixon to oversee the overall business integration project on a full time basis. Mills pf. at 17.

61. One of the critical success factors for any large business affecting system implementation is a dedicated executive sponsor with commitment to make the project successful. The level of commitment and investment that FairPoint has made in this area is exemplary. Mills pf. at 17–18.

62. Prior to the cutover, FairPoint appropriately plans to merge the conversion team with the permanent organization. Wheaton pf. at 25.

63. FairPoint has enlisted the assistance of Capgemini in the transition process; Capgemini is an international firm engaged in consulting, technology services and outsourcing. Haga pf. at 5.

64. Capgemini has experience spanning thirty years in telecom processes and systems design, implementation and operation support, and has served major telecommunications companies in the United States and around the world. Haga pf. at 5; Haga/Kurtze reb. pf. at 4–7.

65. Capgemini is an industry leader in telecommunications consulting and in systems integration. Tr. 9/19/07 at 10 (Kurtze).

66. Capgemini has a workforce of 60,000 around the globe, including 3,500 in its Telecom, Media and Entertainment practice group, and it has a 30-year track record of working with wireline, wireless, Internet service provider ("ISP") and cable companies, among others. Haga pf. at 7.

67. The Capgemini team supporting FairPoint is led by executives and comprised of members with significant experience in the telecommunications industry and systems generally. Capgemini's full-time project manager for the FairPoint project is experienced in managing large complex projects. Haga pf. at 7; Mills pf. at 18.

68. Capgemini provides several layers of expertise: it employs team members who are familiar with and have dealt with the applications that would be purchased, developed and

implemented by or on behalf of FairPoint; professionals whose expertise lies in data center operations and construction of the infrastructure necessary to run these systems; professionals with expertise in the integration area; and professionals experienced in project management. Haga/Kurtze reb. pf. at 5–6.

69. Capgemini is responsible for obtaining, configuring, testing and implementing the FairPoint applications that will serve as the back-office operating environment. Capgemini will also perform data conversion activities and work with FairPoint to establish short and long-term training plans. Haga pf. at 9.

70. Aside from the Capgemini contract, FairPoint does not have a seasoned expert who has either managed or monitored a systems development and conversion effort of the current scale. Wheaton pf. at 25.

b. Discussion

FairPoint has experience operating telephone companies and providing DSL services to customers. While its management team had not been completely assembled at the time of our technical hearings, the FairPoint witnesses demonstrated a thorough understanding of the challenges facing them.

FairPoint's collaboration with Capgemini strengthens its technical competence. Capgemini is one of the largest telecommunications consulting firms in the country and has a wealth of experience with projects of the size and complexity of the anticipated conversion from Verizon to FairPoint. Capgemini has staffed the project with team members who are familiar with and who have dealt with the applications that will be purchased, developed, and implemented by FairPoint. The Capgemini team has the necessary data center operations, systems integration and infrastructure development skills.

We conclude that FairPoint, as augmented by Capgemini, has the necessary experience and has deployed the people needed to successfully develop and implement the systems infrastructure required to support the combined company. FairPoint has the knowledge, experience, and ability to provide the intended services.

3. Business Reputation

a. Positions of the Parties

FairPoint maintains that it has an excellent reputation. It asserts that financial analysts and credit rating agencies have great confidence in FairPoint's ability to manage the combined company and to maintain financial stability.[55]

The Department argues that FairPoint has a sound business reputation in the investment community, and, for the most part in the regulatory jurisdictions in which it operates.[56] The Department also reports that FairPoint's management team is respected, and the financial community expects FairPoint to generate significant cash flow to meet capital investment and dividend requirements.[57] The Department also gives FairPoint "high marks for the openness it has exhibited in communicating and responding to concerns the Department has voiced."[58] The Department expresses two reservations. First, the Department argues that FairPoint does not yet have in place adequate staff to successfully complete this transition.

The Department's second reservation is that, although FairPoint has an excellent reputation generally with state regulators, that is not the case for FairPoint Vermont's operations in Maine and Vermont. The Department criticizes FairPoint's record in Vermont for service quality and customer service. As to Maine, the Department points to a survey that reports regulatory dissatisfaction. FairPoint disputes the Department's interpretation of the survey results from Maine.

One Communications argues that FairPoint does not have a good business reputation in that it will be unable to deliver high quality wholesale service.[59] Specifically, One Communications argues that FairPoint has an unacceptably high level of retail customer complaints in both Maine and Vermont and has made no binding promises to improve service quality. Finally, One Communications argues that FairPoint has no experience providing services to wholesale customers.

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55. FairPoint Brief at 25.
56. DPS Brief at 73.
57. DPS Brief at 72.
58. DPS Brief at 73.
59. One Communications Brief at 16.

b. Findings

71. The Huron Consulting Group interviewed financial analysts and credit rating agencies regarding the company's financial condition and reputation. Lafferty pf. at 24.

72. The financial agencies interviewed all reported confidence in FairPoint's ability to manage the acquired operation and remain financially stable in the process. Lafferty pf. at 28.

73. Wall Street has commended FairPoint's senior management's financial acumen, discipline, experience and savvy. Tr. 9/21/07 at 114 (Wheaton); Wheaton pf. at 25.

74. The financial community believes FairPoint has a cohesive strategy and a proven track record in acquiring properties and operating them effectively. Exh. DPS-FWL-DIR-2 at 3; Wheaton pf. at 24.

75. The FairPoint management team is respected and the financial community expects that FairPoint will generate significant cash flow to meet capital investment and dividend requirements. Lafferty pf. at 28.

76. The financial community has concluded that FairPoint will be successful in completing this transaction and managing the newly acquired properties successfully. The financial community took note of FairPoint's use of the Reverse Morris Trust, its effective management of negotiations with Verizon, its experience in successfully completing numerous acquisitions in the past, its selection of Capgemini as a partner, and its use of lessons learned from its own experience and that of others. Wheaton pf. at 26.

77. FairPoint is well respected by regulatory and other governmental agencies in states outside of Vermont where FairPoint currently operates as an Incumbent Local Exchange Carrier ("ILEC"). Lafferty pf. at 6, 28.

78. On behalf of the Department of Public Service, the Huron Consulting Group conducted a survey of FairPoint's business reputation among regulatory agencies. The survey covered: service quality in general; broadband service quality; accessibility of company personnel; knowledge of company personnel; frequency and type of complaints about the company; and level of interaction between the company and the regulatory agency. Lafferty pf. at 23–24; exh. DPS-FWL-DIR-2.

79. The small size of FairPoint's existing operating companies may have produced less regulatory attention in some states. Lafferty pf. at 23; tr. 9/20/07 at 273 (Lafferty).

80. In the survey, FairPoint received high marks for service quality, broadband deployment and knowledgeable personnel. Lafferty pf. at 7, 25; tr. 9/20/07 at 276 (Lafferty).

81. In all cases, survey respondents who reported direct interaction with FairPoint personnel had favorable experiences. See tr. 9/20/07 at 267 (Lafferty); *see* Lafferty pf. at 25.

82. With the exception of Maine, to the extent surveyed regulators and other government agencies have had opportunities to work with FairPoint, they all report positive experiences. FairPoint's quality of service, broadband service and accessibility and knowledge of personnel are rated above average in most cases. Lafferty pf. at 23; tr. 9/20/07 at 271–272 (Lafferty).

83. In the survey, the Missouri Office of Public Counsel reported that FairPoint had been extremely cooperative and helpful in assisting the state to resolving problems with the Cass County Telephone Company, which FairPoint acquired. The office also reported that FairPoint's service levels and personnel contacts were excellent, and the office was not aware of any litigation, major complaints or labor problems with FairPoint. Exh. DPS-FWL-DIR-2 at 15.

84. The survey disclosed that the New York Department of Public Service had recently commended all three FairPoint ILECs in New York for exemplary service quality. Exh. DPS-FWL-DIR-2 at 15.

85. In Maine, FairPoint is the second largest local telecommunications service provider. It serves approximately 60,000 customer access lines. Maine regulators reported significant concerns with the Company's service quality and level of complaints. Lafferty pf. at 23.

86. The Maine Public Utilities Commission ("Maine PUC") did not provide qualitative information or opinions concerning FairPoint's service or personnel because of ongoing proceedings. It did provide a record of the number of complaints filed against FairPoint. Exh. FP-Cross-12; tr. 9/20/07 at 269–270 (Lafferty).

87. In Maine, complaint levels regarding FairPoint increased significantly in 2005 and 2006. In 2004, FairPoint only had 31 complaints; however, in 2005 and 2007 the number increased to 76 and 70, respectively. The trend in complaints appears to be lower in 2007. The Consumer

Assistance Division of the Maine PUC claims that FairPoint's level of complaints is above the level for other carriers. Lafferty pf. at 25–26; exh. FP-Cross-12.

88. The Maine Public Advocate office also responded to the survey. It characterized FairPoint's performance in Maine as "bad," although it did not provide any information on FairPoint's quality of service, personnel, litigation or labor issues. Exhs. DPS-FWL-2 at 14; FP-Cross-12.

89. In recent years FairPoint appears to have had significant service complaints and problems in Maine and Vermont stemming at least partially from challenges associated with system conversions. Lafferty pf. at 23.

90. In Vermont, FairPoint will be required to convert all the customer service, billing and many other system platforms from the Verizon systems to a new platform after close for the acquired Verizon Vermont (and Maine and New Hampshire) properties. Lafferty pf. at 23.

c. Discussion

We agree with the Department; the record shows that FairPoint has a good reputation in nearly all state commissions and in the financial community. There is no evidence of malfeasance or financial irregularities in the past of either the company or its management. We expect that FairPoint's solid reputation also will apply to its operation of the properties it seeks to acquire.

Although FairPoint has had some difficulties in both Maine and Vermont arising from billing conversions, that does not appear to be a basis for concluding that the company is not a suitable business partner for Vermont customers.

One Communications' objections are largely questions of customer service, not business reputation. We discuss these issues below in Part V.D.3.

We reject One Communications' argument that the absence of prior wholesale services experience prevents FairPoint from demonstrating a good business reputation. Inexperience by itself might be an issue for an entirely new and unknown entrant, but FairPoint is an established company that has provided retail services in Vermont and other states for years. While this merger would expand its operations greatly, we know a great deal about the company and its management. In essence, One Communications is asking us to rule that because FairPoint has never yet provided the kind of wholesale services to CLECs that Verizon today offers, it cannot have a good reputation in doing so and should be denied entry into that field. While this expanded wholesale role certainly presents risks to CLECs, we have taken great care to deal with those risks elsewhere in this Order. We decline to establish a precedent that an otherwise reputable company enter a new field of services simply because it is new in that field.

We conclude that FairPoint satisfies our requirement that a new entrant must have a good business reputation.

4. Other Regulatory Approvals

a. Positions of the Parties

The Department recommends, in DPS condition number 45, that FairPoint be required, prior to closing, to update the Board and Department on the FCC approval status for the license transfers under section 310(d) of the FCC's rules and the section 214 authorizations. In addition, the Department recommends that final approval of the acquisition in Vermont should be conditioned on FairPoint obtaining the required approvals from the FCC. FairPoint agrees to this condition.[60]

The Department also recommends, in DPS condition number 46, that FairPoint and Verizon should provide notice to the Board and Department of receiving regulatory approval in Maine and New Hampshire prior to closing on the transaction in Vermont. In the alternative, FairPoint and Verizon should be required to obtain specific Board approval to close the Vermont portion of the acquisition without closing the Maine and New Hampshire portions. FairPoint agrees to this condition.[61]

b. Findings

91. FairPoint and Verizon also have filed an application with the Federal Communications Commission ("FCC") for the transfer of licenses under sections 214 and 310(d) of the

60. FairPoint Reply Brief at 16.
61. FairPoint Reply Brief at 16.

Communications Act of 1934 for approval to serve in Maine, New Hampshire and Vermont. The section 214 authorizations cover both domestic and international operating authorities for the acquired properties. Lafferty pf. at 8.

92. The Proposed Transaction must be approved by several other regulatory bodies in addition to the Board, including the FCC, the New Hampshire Public Utilities Commission and the Maine PUC. Tr. 9/6/07 at 132 (Leach); Lafferty pf. at 8.

93. The Proposed Transaction also requires a filing with the U.S. Department of Justice and the Federal Trade Commission under the Hart-Scott-Rodino Antitrust Improvements Act of 1976. Tr. 9/6/07 at 132 (Leach).

94. Various state and FCC approvals are still pending. Lafferty pf. at 8; tr. 9/6/07 at 132–133 (Leach).

95. The parties' merger agreement is conditioned on obtaining all regulatory approvals. Skrivan reb. pf. at 23; tr. 9/6/07 at 132 (Leach); tr. 9/7/07 at 227 (Skrivan).

96. FairPoint has requested a waiver of sections 61.41 (b) and (c) of the FCC's rules – the "All or Nothing Rule." The purpose of this request is to allow FairPoint to continue operating its existing FairPoint Vermont operations pursuant to rate of return regulation for federal regulatory purposes. Since the acquired Verizon properties are subject to the FCC's price cap rules, absent the waiver the FCC rules would require FairPoint to convert its "classic" properties to price cap regulation. In the alternative, FairPoint could make a one-time election to withdraw the acquired properties from price cap regulation. However, in its waiver filing with the FCC, FairPoint has stated that it intends to operate the Verizon properties under the price cap rules. If FairPoint is required to file price cap tariffs for its "classic" properties, it is possible the price cap mechanism would reduce the Company's revenues. Lafferty pf. at 9.

97. FairPoint has been able to invest significant funds in broadband technology and service quality for its "classic" properties. The rate of return mechanism has allowed FairPoint to receive a reasonable return on some of these investments, which, given the low density of the territories and associated higher costs, may not have been possible under price cap regulation. Lafferty pf. at 9.

98. The current level of universal service support available to price cap companies might be insufficient if the "classic" FairPoint properties came under the price cap rules. If universal support is reduced, it is possible investments in broadband deployment and service improvements in rural markets would be reduced which could harm customers in Vermont and elsewhere. Lafferty pf. at 10.

c. Discussion

We agree with the Department's recommendations regarding approvals by other regulatory bodies, but clarification is needed. Requiring approval here after imposition of conditions in the other states should not be an alternative to notifying us of those states' actions. Conditions imposed by other states may have a direct impact upon our conclusion on the merits of the Proposed Transaction. Therefore, we restate the Department's proposed condition to require review by the Board if the other states or the FCC impose conditions. Because possible conditions from the FCC present the same issues, if we were to approve the merger, we would include FCC approvals and state approvals together in the following conditions.

> **If FairPoint and Verizon receive conditional or unconditional regulatory approval from the FCC, the Maine Public Utilities Commission or the New Hampshire Public Utility Commission, FairPoint and Verizon shall provide notice to the Board and Department and a copy of the relevant orders.**
>
> **If regulatory approvals from the FCC, the Maine Public Utilities Commission or the New Hampshire Public Utility Commission is conditional, approval in Vermont is conditioned upon subsequent review by this Board of the conditions imposed by those other regulatory bodies. The partes may not close the transaction until that subsequent Vermont review has been completed. The Board will provide an expedited procedure to review any such conditions.**

C. Financial soundness

1. Position of the Parties

a. FairPoint

FairPoint maintains that the telecommunications industry is changing from its focus from voice products to wireless and data products.[62] Based largely on a detailed cash flow projection, FairPoint argues that the proposed merger will leave the surviving corporation financially sound.[63] Specifically, FairPoint projects its free cash flow to be relatively stable at approximately $200 to $220 million annually over the first five years after closing.[64] Of this, FairPoint plans to distribute $142 million every year as dividends to shareholders, or between 65% to 71% of its free cash flow.[65]

This would leave cash after dividends, or to use FairPoint's term, a "cash flow cushion" of about $70 million annually, for a cumulative cushion of $483 million to be accumulated from 2008 through 2015.[66] This cushion, FairPoint argues, will provide a substantial buffer against unexpected difficulties that can support investments to improve customer service, to increase broadband access[67] or to reduce cash interest expenses.[68]

FairPoint maintains that this cash flow projection is based on reasonable, even conservative, assumptions.[69] FairPoint asserts that it has taken account of anticipated "healthy competition" with cable competitors and other telecommunications providers.[70] FairPoint argues that its projected line losses, operating expense savings and capital structure are within the range of the observed historical performance of comparable guideline companies.[71]

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62. FairPoint Brief at 59, 74.
63. *See* exh. DPS-PLW-DIR-2, ("Discovery Model"). The Discovery Model reports revenues separately for its "FairPoint" operations, for its "Spinco" operations resulting from the merger, and for the combined or "pro-forma" company totals.
64. FairPoint Brief at 60–61.
65. FairPoint Brief at 61.
66. FairPoint Brief at 61.
67. FairPoint Brief at 61.
68. FairPoint Brief at 61.
69. FairPoint Brief at 63, 72; Reply Brief at 20–21.
70. FairPoint Brief at 75.
71. FairPoint Brief at 62, 75.

FairPoint also argues that financial markets will judge it in comparison to its peer mid-sized telephone companies, and that the projections for the northern New England operations compare favorably with benchmark metrics observed in comparable guideline companies.[72] FairPoint contends that it is likely to outperform those projections because of additional opportunities, such as by earning larger revenues per line or by further cutting cash operating expenses.[73] It also notes that in earlier acquisitions, it has always outperformed its pre-acquisition financial projections.[74]

Although FairPoint acknowledges the likely continuation of access line losses, it expresses confidence that its competitive focus will reduce that rate of that loss.[75] FairPoint believes that it is "well-poised" to compete against cable and is aware of cable competition from entities such as Comcast in Vermont.[76] Even if line losses are greater than expected, FairPoint argues that its cash buffer will be large enough to avoid any harm.[77]

FairPoint maintains it has established an optimal financial structure by obtaining all financing through the parent company. This structure does not directly encumber the assets of the operating company. FairPoint argues that it also minimizes the cost of debt.[78]

FairPoint has commitments for approximately $2.1 billion of the $2.4 to $2.5 billion it needs to close the transaction.[79] FairPoint anticipates repaying a substantial amount of bank debt by 2012 and keeping its debt levels within the limits set by covenants and dividend restrictions imposed by lenders.[80]

FairPoint anticipates paying substantial dividends to shareholders, but it contends that this plan is within a range required by the capital markets and compares favorably to industry peers.[81] It maintains, however, that dividends are discretionary and can serve as an "emergency cushion if

72. FairPoint Brief at 62.
73. FairPoint Brief at 62–63, 75
74. FairPoint Brief at 73–74.
75. FairPoint Brief at 65.
76. FairPoint Brief at 66.
77. FairPoint Brief at 65.
78. FairPoint Brief at 67, 75.
79. FairPoint Brief at 67.
80. FairPoint Brief at 68.
81. FairPoint Brief at 69.

needed."[82] Instead, FairPoint contends that "in the case of an unexpected natural disaster or some other non-recurring event, FairPoint's cash flow will first be used to assure continuing service to customers."[83] In the face of unforeseen financial pressures, FairPoint argues that its focus will be on preserving its core operations, which are the source of long-term value for its employees, customers, and financial stakeholders.[84]

FairPoint has agreed to limit dividends if FairPoint violates any of four specified standards. The first three replicate bank covenants relating to debt leverage, interest coverage, and cumulative cash flow. The last would prohibit FairPoint from declaring dividends if it had not met specified capital expenditure targets in Vermont.[85] The restrictions would expire on December 31, 2010, the end date of the Amended Vermont Incentive Regulation Plan.

b. Department

The Department states that it does not "wish to suggest" that FairPoint's "business model is doomed to fail" or that it "must necessarily be judged to be financially unstable and unsound."[86] Also, the Department asserts that FairPoint's financial projections indicate

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82. FairPoint Brief at 69 (proposed finding 280) (internal quotes omitted).

83. FairPoint Brief at 69 (proposed finding 280).

84. FairPoint Brief at 71.

85. FairPoint agrees to the following dividend restrictions:

a. Dividends are prohibited if the debt leverage test (total debt divided by Earnings before Interest, Taxes, Depreciation, and Amortization ("EBITDA")) exceeds 5.75 to 1.0 during the first year following the closing and thereafter 5.50 to 1.0. This restriction protects against the accumulation of excessive debt levels.

b. Dividends are prohibited if the interest coverage test (EBITDA divided by total interest expense) drops below 2.25 to 1.0. This restriction protects against both the accumulation of excessive debt and a rise in interest rates.

c. Dividends are prohibited if dividend payments exceed the cumulative free cash flow generated by the company following the closing (subject to the same calculation and determination provided in the final bank credit agreement). This restriction protects, over time, against the possibility that more could be paid out in dividends than was generated in cash flow.

d. Dividends are prohibited if, following the two-year and three-year anniversaries of the closing, the annual capital expenditures in Vermont average less than $41 million over two years or $40 million over three years. FairPoint Brief at 70, 75–76; tr. 9/5/07 at 94–99 (Leach); exh. FP Cross 1, 3.

86. DPS Brief at 59.

"sufficient cash flows to fund its capital program and provide an acceptable level of customer service for the period from 2008 to 2015."[87]

On the other hand, the Department apparently concludes that FairPoint has not established the accuracy of its financial projections[88] and that its financial stability and soundness cannot be assured absent specific safeguards.[89] The DPS also maintained that if rate of return regulation were to be resumed after the closing, FairPoint's Vermont properties would be "unlikely to be financially viable," unless the Board both allowed FairPoint to earn a return on the premium it paid to Verizon above net book value and imputed a capital structure that includes some level of equity.[90]

The Department clearly perceives risk in the transaction. It asks the Board to protect Vermonters from the risk that free cash flow generated by the Vermont operations would be "diverted from service quality and capital expenditure initiatives to satisfy FairPoint's heavily leveraged capital structure and investor dividend payout policy."[91] The Department proposes conditions aimed at monitoring this cash flow upwards to the FairPoint parent company, including a requirement that the Vermont operating company be a separate legal entity and that FairPoint establish "safeguards" regarding all significant cash transactions.

The Department conducted sensitivity analyses of FairPoint's financial projections.[92] The results, maintains the Department, show that FairPoint's financial viability is very sensitive to changes in revenue. These changes could occur as a result of competition or changes in regulatory treatment, or some combination of both.[93] Further, the Department asserts that at

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87. DPS Brief at 55 (proposed finding no. 216).

88. DPS Reply Brief at 6 (Wheaton testimony raised numerous questions about whether FairPoint's business case will ultimately be borne out).

89. DPS Brief at 59.

90. DPS Brief at 56 (proposed finding no. 224).

91. DPS Brief at 59.

92. The Department first assumed that FairPoint's initial revenues would be significantly less than FairPoint anticipated. Then the Department modified the company's operations using seven hypothetical scenarios. Jeanson sur. pf. at 2–3.

93. DPS Brief at 57.

some time before the end of 2015, it is likely that FairPoint will have to reduce dividend payments for one or more years in order to remain in compliance with its debt coverage ratios.[94]

The Department also criticizes FairPoint's assumptions about future rates. FairPoint, asserts the DPS, has "failed to consider the possibility that the Incentive Regulation Plan might not be extended in 2010 and that its rates could become subject to traditional cost-of-service based ratemaking."[95] The Department further argues that FairPoint seems not to understand the degree to which FairPoint is depending on a future Board to impute (1) a rate base that includes an acquisition premium and (b) a capital structure that includes some hypothetical level of non-existent equity. The Department characterizes FairPoint as "disturbingly uncurious about whether this expectation comports with the Board's past practices in the regulation of Vermont utilities."[96] Significantly, the Department also requests a finding that, should rate-of-return ratemaking be resumed after closing, FairPoint would not be financially viable without allowing recovery on at least a portion of its "goodwill," or the premium that FairPoint paid above rate base.[97]

The Department supports the imposition of four significant conditions aimed at keeping sufficient cash within a Vermont operating company.[98] The conditions, numbered according to the original DPS system, are:

- # 4: Mandate a separate legal entity to separate all Vermont related assets and liabilities, if any, from the assets and liabilities of other FairPoint regulated, non-regulated and classic operations.
- # 5: Require FairPoint to file in advance with the Department and Board copies of contracts with affiliates worth $25,000 or more. Copies would be filed 30 days in advance. All such contracts would be required to be based upon arms-length negotiations.
- # 6: Require FairPoint to establish safeguards regarding the outflow and transfer of cash including dividends and loans of any form from the separate Vermont entity for the

94. DPS Brief at 56.

95. DPS Brief at 56 (proposed finding nos. 223, 225).

96. DPS Brief at 58.

97. DPS Brief at 56 (proposed finding no. 224).

98. Exh. DPS-CJC-5. In proposed condition # 8, the Department also proposed barring FairPoint from attempting to recover transaction-related and transition-related expenses in future rate proceedings. We discuss that recommendation in Section V.D.1., below.

acquired Vermont regulated operations to the FairPoint Parent Company or other affiliates. Such safeguards could include thirty-day advanced notification to the DPS and the Board of all planned loans, dividends and cash transfers of any kind from FairPoint - Vermont to other FairPoint entities. Suspension of the cash transfers, dividend payments and loans could then be required by the Board if it were determined that FairPoint was not consistently meeting its commitments related to service quality minimum standards; effectively managing its Vermont regulated operations; or meeting the broadband build-out commitments.

- # 7: Require the newly-acquired FairPoint properties in Vermont to provide specific tracking and annual reporting (by FCC Account) for the next seven years of the estimated savings that FairPoint's new Vermont operation and FairPoint Communications anticipate and realize from the merger. An annual report of savings and cost avoidance would be provided to the Board and the Department within forty-five days after the close of the calendar year.

The Department also argues that FairPoint has not adequately demonstrated a commitment to maintain an adequate rate of capital investment in Vermont.[99] The Department explains that it sought a separate subsidiary in part to obtain an enforceable commitment from FairPoint on capital expenditures.[100]

c. Labor

Labor Intervenors argue that FairPoint does not have the financial resources to provide reliable service and continue to make necessary capital investments. Labor argues that financial projections show that FairPoint would be under financial stress soon after the proposed transaction is consummated, and that its financial condition would continue to deteriorate over time. Labor contends that FairPoint has made flawed assumptions with respect to operating expenses and from paying more in dividends than net income.[101] Labor also argues that FairPoint's assumptions about operating expense savings, particularly savings related to employee attrition, are overly optimistic. Further, Labor noted that FairPoint's financial condition would deteriorate over time because FairPoint plans to pay out between 200 and 300 percent of projected net income as dividends.

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99. DPS Brief at 53.
100. DPS Brief at 54.
101. Labor Brief at 11.

Even if FairPoint's assumptions were made to be more realistic, Labor argues that FairPoint would still experience financial hardships shortly after the proposed closing. On the basis of its analysis, Labor contends that FairPoint is not financially sound and is too small, too inexperienced and too thinly capitalized to pursue this transaction.[102] Thus, Labor recommends that the Board deny the Joint Petitioners' request.

d. One Communications

Relying on the testimony of Labor's witness, One Communications states that the record clearly indicates that the acquiring company is not financially sound, and that the combined company would also be financially weak.[103] One Communications supports Labor's contention that FairPoint had little choice but to pursue this transaction in order to remain viable and satisfy its stockholder demands. One Communications also points to the amount of debt that the combined company would assume as support for the contention that FairPoint would be a financially weak carrier and would not be able to make good on all of the promises, including promises from FairPoint's management to wholesale customers.

e. Sovernet

Sovernet claims that FairPoint failed to demonstrate that it would have the financial resources to provide unbundled network elements and interconnection services to wholesale customers. Sovernet relies on a June 5, 2007, Morgan Stanley report stating that FairPoint would not be able to generate sufficient cash flow to cover its dividend in 2008.[104] As a result, Sovernet expresses concern that FairPoint would not be able to provide adequate services to wholesale customers.[105]

102. Labor Brief at 17.
103. One Communications Brief at 7.
104. Sovernet Brief at 28; referring to exh. DPS-Cross-15.
105. Sovernet Brief at 25–28.

f. FairPoint's Reply

Disagreeing with the Department, FairPoint contends that it has fully considered the rate-making implications of future regulatory decisions.[106] FairPoint also argues that the Department overlooked the possible effect of declining revenues on traditional cost-of-service methodologies. FairPoint acknowledges that because a Vermont operating company would have a 100% equity capital structure, a hypothetical capital structure would be imputed.[107] FairPoint notes that the Department's "own witness, Mr. Jeanson modeled the effects of rate decreases in Maine and Vermont and determined that FairPoint would remain financially sound even in the event of such decreases and other adverse events."[108] Finally, FairPoint argues that the present proceeding is not a rate case, and the record does not provide for any meaningful consideration of what a revenue requirement would be in 2010.

FairPoint also contends that the Department has inappropriately relied on decisions from other state commissions. FairPoint argues that commission decisions in New York and Illinois were based on different factual circumstances, notably company size, and established different conditions.[109]

Nonetheless, in its Reply Brief, FairPoint has agreed to most of the conditions proposed by the Department. In Proposed Condition #4, the Department proposed a separate legal entity. FairPoint does not think a separate entity is necessary, and it would be costly. However, FairPoint agrees to form a separate Vermont entity to hold the regulated Vermont telecommunications assets for the acquired Vermont operations.[110]

In Proposed Condition #5, the Department proposed requiring FairPoint to develop all significant contracts with affiliates at arms length and to file advance copies with the Department and Board. FairPoint agrees with this condition.[111]

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106. FairPoint Reply Brief at 22.
107. FairPoint Reply Brief at 22.
108. FairPoint Reply Brief at 22–23.
109. FairPoint Reply Brief at 23.
110. FairPoint Reply Brief at 7.
111. FairPoint Brief at 104 (finding 397); FairPoint Reply Brief at 7.

In Proposed Condition #7, the Department proposed requiring FairPoint to perform annual financial reporting by FCC account for seven years. FairPoint agrees with this condition.[112]

In Proposed Condition #6, the Department proposed requiring FairPoint to adopt safeguards for cash transfers, including suspension of cash payments if FairPoint was not meeting particular commitments.[113] FairPoint disagrees with this proposal, arguing that the condition is not consistent with the intent and terms of the financing for the proposed transaction and ultimately would jeopardize the closing of the transaction itself. FairPoint also argues that the financing for the proposed transaction does not contemplate any restrictions on dividend payments from the acquired entities to the parent company and ultimately would require FairPoint to renegotiate the terms of its financing.[114]

Instead, FairPoint supports the alternative restrictions, discussed above, that include meeting its various lender covenants and suspending dividends in the event of insufficient capital expenditures in Vermont.[115] FairPoint particularly objects to restrictions on cash flow between a Vermont operating entity and the parent. It argues that since all of the debt of the corporation will be held at the parent company level, it must ensure that adequate funds are available to service the parent company debt, and no encumbrances of any kind should restrict the flow of cash payments from the Vermont entity or operations to the parent company.[116]

FairPoint did restate and slightly expand its fourth proposed condition in its Reply Brief. This version is consistent with FairPoint's offers in Maine and New Hampshire. As restated:

> To ensure investment in the network occurs as projected by FairPoint, total dividend payments from FairPoint to its shareholders following the two year anniversary of the closing will be reduced the following year by the amount in which the annual average capital expenditures made in Vermont over the two years is less than $41 million and dividends paid in the year following the three

112. FairPoint Reply Brief at 7.

113. The Department's proposed cash and dividend restriction would be triggered if it were determined that FairPoint was not consistently providing quality service, effectively managing its Vermont regulated operations and deploying broadband facilities.

114. FairPoint Reply Brief at 18–19, 26.

115. FairPoint Reply Brief at 26–29.

116. FairPoint Reply Brief at 26.

> year anniversary will be reduced by the amount in which the annual average capital expenditures over three year period is less than $40 million.[117]

Further, FairPoint agrees to keep a specified amount of its credit facilities available specifically for use in Vermont as a way to assure liquidity will be available to the state operations at all times.[118]

2. Findings

a. Financing

99. The total value to be received by Verizon and its stockholders in this transaction will be approximately $2.715 billion. This price is funded by a combination of $1.015 billion in equity (37% of price) and $1.7 billion of debt (63% of price). Leach pf. at 15.

100. The number of shares FairPoint will issue as part of the transaction is fixed; if FairPoint's stock price falls, Verizon shareholders will receive less value. Tr. 9/6/07 at 91 (Leach).

101. FairPoint plans to acquire debt of $2.5 billion to close the transaction. As of September, 2007, it had commitments for approximately $2.1 billion. This includes:

a. $0.8 billion through a fixed-rate bond that will effectively go to Verizon;

b. $1.1 billion through other variable rate bank loans; and

c. $0.2 billion through a revolving loan that FairPoint does not expect to use.

Tr. 9/5/07 at 78 (Leach); tr. 9/6/07 at 92–94 (Leach).

102. Of its $2.1 billion of current bank commitments, FairPoint only expects to use $1.7 billion. If this occurs, FairPoint would have a $400 million cushion within its current bank commitments. Tr. 9/6/07 at 92–93 (Leach).

103. FairPoint also plans to borrow an additional $400 million to $500 million in order to reach the total of $2.5 billion needed for closing. FairPoint has not yet decided between bank debt and bonds. Tr. 9/5/07 at 78 (Leach).

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117. FairPoint Reply Brief at 27; Leach reb. pf. at 65 (offering reasonable annual capital expenditures "until the Board has evidence the performance criteria have been met"); *see* tr. 9/5/07 at 98 (Leach).

118. Tr. 9/20/07 at 212 (Nixon); Leach reb. pf. at 64–65.

104. Other than the bond, the bank commitments are subject to variable interest rates that will float over the London Interbank Offered Rate ("LIBOR"). Adding together FairPoint's planned fixed rate bond and its existing interest-rate swaps in existence in September, 2007, FairPoint anticipated that approximately 60 to 65% of its loans would be at fixed rates. A higher percentage may be arranged closer to the time of closing. Tr. 9/5/07 at 79–81 (Leach).

105. It has not been difficult for FairPoint to find parties for possible interest rate swaps, and it typically can choose from among multiple bids. Tr. 9/6/07 at 89 (Leach).

106. Any changes that made the high-dividend model less attractive or less efficient would cause FairPoint to adopt another capital structure that produced a more efficient capital structure. Tr. 9/6/07 at 212–213 (King).

107. The Reverse Morris Trust ("RMT") financing approach that Verizon and FairPoint propose will enable FairPoint to acquire the Verizon New England properties at a lower price. The RMT results in a tax-free transaction for the shareholders of Verizon and allows Verizon to accept a lower price. The RMT is an appropriate method for acquiring and capitalizing a regulated utility. Other telecommunications companies have recently completed similar tax-free transactions. Wheaton pf. at 11–12; Nixon pf. at 9; Leach pf. at 15; Balhoff pf. at 11–13.

108. FairPoint is subject to debt covenants. Violation of either of the following covenants would require FairPoint to limit dividends to shareholders.

a. The first dividend restriction prohibits dividend payments if the debt leverage test (total debt divided by EBITDA) exceeds 5.75 to 1.0 during the first year following the closing and thereafter 5.50 to 1.0. This restriction protects against the accumulation of excessive debt levels.

b. The second dividend restriction prohibits dividend payments if the interest coverage test (EBITDA divided by total interest expense) drops below 2.25 to 1.0. This restriction protects against both the accumulation of excessive debt and a rise in interest rates.

Exh. FP Cross-3; tr. 9/5/07 at 95–97 (Leach); Jeanson reb. pf. at 6.

b. Shareholder's Equity

109. FairPoint's beginning shareholder equity in 2008 is $298 million. This is a low figure in large part because of the nature of the RMT that is the vehicle for the acquisition. Exh. DPS - PLW Dir 2, Section I, pg. 4; tr. 9/5/07 at 36 (Leach).

110. FairPoint plans to decrease its shareholder equity every year. This will occur because the company plans to pay shareholders substantially more dividends than the company's earnings. FairPoint projects the following earnings, dividends and equity through 2015 (millions):

Year	2008	2009	2010	2011	2012	2013	2014	2015
Net Income	($28)	$47	$57	$57	$56	$61	$64	$66
Dividends	$142	$142	$142	$142	$142	$142	$142	$142
Shareholder Equity	$130	$36	($48)	($133)	($218)	($298)	($376)	($452)

Exh. DPS-PLW Dir 2, Section I, at 2-4; *see* tr. 9/20/07 at 202–203 (Nixon).

111. The RMT vehicle could produce a negative book equity, thereby causing a conflict with the traditional rate of return ratemaking used in the utility industry. Rate of return ratemaking allows utilities an opportunity to earn a reasonable return on rate base book value. In a rate of return environment, FairPoint might become insolvent unless it receives an imputed value for the price paid to acquire the properties. Wheaton pf. at 12–13; Behrns sur. pf. at 7–9 and 11–13.

112. FairPoint has disclosed to its investors in its SEC S-4 statement numerous risks associated with the Proposed Transaction that could materially affect the company's financial stability and soundness. One of those risks is that FairPoint's high level of debt could require a significant portion of the company's cash flow from operations to be dedicated to the payment of interest, and to a lesser extent, principal, thereby reducing funds available for future operations, dividends on common stock, capital expenditures, or acquisitions. Exh. DPS-Cross-6; tr. 9/5/07 at 88 (Leach).

c. Projected Cash Flow

113. On a combined basis, comprising both Northern New England acquisition and the existing FairPoint Vermont companies, FairPoint projects the following net cash flow after projected capital expenditures and dividend payments (millions).

Year	2008	2009	2010	2011	2012	2013	2014	2015
Net Cash from Operating	$295	$389	$383	$372	$360	$345	$333	$323
Capital Expenditures	($325)	($167)	($164)	($159)	($157)	($156)	($156)	($156)
Dividends & Investing Costs	($142)	($142)	($144)	($142)	($142)	($142)	($142)	($142)
Net Increase in Cash Balance	($172)	$80	$75	$71	$61	$47	$35	$25

Exh. DPS-PLW-2, Section I, pg. 4.

114. If FairPoint's financial projections are realized, it will have sufficient cash flows to fund its capital program and provide an acceptable level of customer service for the period from 2008 to 2015. Wheaton pf. at 9.

115. FairPoint anticipates the following Internet Service Provider revenues, expenses and net profits for its NNE operations from 2008 through 2015:

Year	2008	2009	2010	2011	2012	2013	2014	2015
ISP Revenue ($M)	99	121	142	146	146	145	144	143
ISP Expense ($M)	126	146	165	178	187	197	206	212
ISP Profit ($M)	(27)	(25)	(23)	(32)	(41)	(52)	(62)	(69)

Exh. DPS-PLW-DIR-2, pages 4, 8, 9, 11.

d. Capital Availability

116. FairPoint has completed numerous acquisitions in the past. Wheaton pf. at 26.

117. FairPoint's stock is not and never has been rated as investment grade. FairPoint has no plans for its stock to become investment grade. FairPoint does not see attaining investment grade as a critical factor in grading shareholder value. FairPoint perceives advantages in being below investment grade because it allows a different mix of debt and equity that creates different shareholder returns. Tr. 9/5/07 at 31–34 (Leach).

118. In order to become an investment grade company, FairPoint would have to attain a book value of shareholders' equity of $1 billion. Wheaton pf. at 14.

119. Most of FairPoint's peer telecommunications companies are also rated below investment grade. Like FairPoint, none of these peer telecommunications companies have a lengthy history

of operating or trading successfully while rated below investment grade. Wheaton pf. at 16; tr. 9/6/07 at 178, 182–183 (King).

120. Generally, the investment community and the rating agencies are more concerned with FairPoint's free cash flow than with its book value. The investment community believes that FairPoint's cash flow projections will ensure that it has sufficient cash flow to fund its capital program and its ongoing operations. Wheaton pf. at 15.

121. The fact that FairPoint will not be an investment grade company at the close of the Proposed Transaction is not expected to inhibit its ability to fund its capital program and provide an acceptable level of customer service to its Vermont customers. Wheaton pf. at 12–13.

122. Moody's Investors Service gave FairPoint a B1 rating in February 2007, with a stable outlook. Comments specific to FairPoint by Moody's indicate that the company's stable rating outlook reflects a belief that FairPoint would be successful in integrating Verizon's NNE operations and will continue to minimize the effect of revenue losses from declining access lines by offering higher-margin high speed data product offerings. Wheaton pf. at 16–17.

123. Moody's February 2007 credit report also indicates that if the integration of the Verizon NNE operations takes longer than expected and FairPoint is unable to realize the projected synergies, then Moody's rating may be reduced. Wheaton pf. at 17.

124. Moody's February 2007 credit report indicates that FairPoint's credit rating may be negatively affected if the number of access lines falls by six percent or more annually and the company is unable to attain revenue growth from complementary products. Wheaton pf. at 17.

125. Standard & Poor's characterized FairPoint's "shareholder-oriented financial policy" as a weakness. It also characterized FairPoint's aggressive capital structure as a weakness, meaning its high ratio of debt to equity, as well as its high dividend rate policy. Exh. DPS-Cross-18 at 3; tr. 9/6/07 at 185 (King).

e. Projected Switched Access Revenue

126. FairPoint projects operating revenues for its existing operations ("FairPoint"), its NNE operations, and its combined operations as follows:

Year	2008	2009	2010	2011	2012	2013	2014	2015
FairPoint Op.Rev. ($M)	275	274	272	269	266	263	260	257
FairPoint Percent Change		-0.5%	-0.5%	-1.2%	-1.2%	-1.1%	-1.2%	-1.2%
NNE Op.Rev. ($M)	1,151	1,145	1,150	1,144	1,138	1,135	1,136	1,136
NNE Percent Change	-2.1%	-0.5%	0.4%	-0.5%	-0.5%	-0.2%	0.1%	0.0%
Combined Op.Rev. ($M)	1,426	1,419	1,422	1,413	1,404	1,398	1,396	1,393
Combined Percent Change		-0.5%	0.2%	-0.6%	-0.7%	-0.4%	-0.2%	-0.2%

Exh. DPS-PLW-2, Section I, pg. 2; Section II, pg. 1.

127. The switched access line counts for Verizon in the NNE operation over the period 2003–2006, excluding UNE-L lines, were as follows:

Year	2003	2004	2005	2006
Switched Access Lines (000)	1,781	1,696	1,608	1,507
Percent Change		-4.8%	-5.2%	-6.3%

Exh. WEK-1, Table 2.1; calculation.

128. FairPoint projects a loss of approximately 299,000 switched access lines in the NNE operation over the planning horizon, as follows:

Year	2008	2009	2010	2011	2012	2013	2014	2015
Switched Access Lines (000)	1,312	1,241	1,184	1,138	1,099	1,066	1,039	1,015
Percent Change	-6.2%	-5.4%	-4.6%	-3.9%	-3.4%	-3.0%	-2.5%	-2.3%

The cumulative loss of access lines during the period shown is 22.6 percent. The cumulative annual growth rate is minus 3.6 percent. Exh. DPS-PLW-2, Section II, pg.1; Leach pf. at 20–21.

129. FairPoint expects retail line losses due to competition from wireless carriers, CLECs, cable Voice over Internet Protocol ("VoIP") providers, and independent VoIP services. In general, line losses from cable competition have been lower in more rural areas. Leach pf. at 21; tr. 9/6/07 at 227–228 (King).

130. FairPoint's financial model assumes that it will have to compete with other providers on price. FairPoint presently competes successfully against cable providers in more than half its markets and has done very well in those markets. Tr. 9/6/07 at 58–59 (Leach) (confidential); tr. 9/6/07 at 137–138 (Leach).

131. FairPoint may outperform its financial projections in two ways. First, FairPoint's projected revenue per line or per connection is below the industry mean and median figures. This suggests FairPoint could improve revenue by 10 to 25 percent. Second, FairPoint's projected cash flow margins are below the industry mean and median and suggest FairPoint could improve these margins by as much as 25 percent through new product offerings. King reb. pf. at 4, 12–13, 25; Leach reb. pf. at 36–38 (discussing EBITDA margin); tr. 9/7/07 at 142–145 (Balhoff) (observing that FairPoint has the potential to significantly outperform its projections).

132. FairPoint plans to introduce a wireless service, which it will provide using an arrangement with a Mobile Virtual Network Operator ("MVNO"). Revenues from the wireless service are projected to grow to around $15 million annually by Year 5. This wireless service could provide additional revenue growth. Leach pf. at 24; tr. 9/6/07 at 117 (Leach).

133. In all of FairPoint's past acquisitions, the acquired companies have exceeded FairPoint's Year 2 adjusted EBITDA projections. Leach reb. pf. at 28–29; King reb. pf. at 28.

134. Verizon's average revenue per access line in 2005 was $730. FairPoint assumes the average revenue per access line will increase during the planning period. Exh. WEK-1; King reb. pf. at 17.

135. If the rate of lost access lines were to remain at a consistent six percent during the planning period ("Steady State Scenario"), FairPoint would have the following access lines and revenues:

Year	2008	2009	2010	2011	2012	2013	2014	2015
Lines - FPT Forecast (000)	1,312	1,241	1,184	1,138	1,099	1,066	1,039	1,015
Loss Rate - Steady State		-6%	-6%	-6%	-6%	-6%	-6%	-6%
Lines - Steady State (000)	1,312	1,233	1,159	1,090	1,024	963	905	851
Lines - difference (000)	0	(8)	(25)	(48)	(75)	(103)	(134)	(164)
Avg Rev per Acc Line	$730	$730	$730	$730	$730	$730	$730	$730
Revenue Effect ($M)	$0	($6)	($18)	($35)	($54)	($75)	($98)	($120)
Projected NNE Op.Rev. ($M)	1,151	1,145	1,150	1,144	1,138	1,135	1,136	1,136
Percent of Proj. Rev. Lost	0%	0%	-2%	-17%	-18%	-19%	-20%	-22%

Findings 126, 128, and 134, above.[119]

136. In areas where cable companies and the incumbent telephone company compete for voice, data and video services, cable companies typically earn between a 25 to 40 percent market share for voice telecommunications. Tr. 9/7/07 at 143–144 (Balhoff), tr. 9/6/07 at 215 (King).

137. If the rate of access line loss were six percent over the same period, but an additional 5 percent loss were to occur in 2009 and 2010 due to the arrival of cable-based VoIP service ("VoIP Scenario"), FairPoint would have the following numbers of access lines and revenues:

Year	2008	2009	2010	2011	2012	2013	2014	2015
Lines - FPT Forecast (000)	1,312	1,241	1,184	1,138	1,099	1,066	1,039	1,015
Loss Rate - VoIP		-11%	-11%	-6%	-6%	-6%	-6%	-6%
Lines - VoIP (000)	1,312	1,168	1,039	977	918	863	811	763
Lines - difference (000)	0	(73)	(145)	(161)	(181)	(203)	(228)	(252)
Avg Rev per Acc Line	$730	$730	$730	$730	$730	$730	$730	$730
Revenue Effect ($M)	$0	($54)	($106)	($118)	($132)	($148)	($166)	($184)
Projected NNE Op.Rev. ($M)	1,151	1,145	1,150	1,144	1,138	1,135	1,136	1,136
Percent of Proj. Rev. Lost	0%	-5%	-9%	-17%	-18%	-19%	-20%	-22%

Findings 126, 128, and 134, above.[120]

f. Projected DSL and Toll Revenues

138. FairPoint projects an increase of approximately 141,000 Digital Subscriber Lines ("DSL") in the NNE operation over the planning horizon, as follows:

Year	2008	2009	2010	2011	2012	2013	2014	2015
DSL Lines (000)	277	314	349	362	375	389	404	419
Percent Change	16.8%	13.3%	11.2%	3.6%	3.7%	3.7%	3.8%	3.6%
Penetration of Retail Lines	23.8%	28.4%	33.1%	35.7%	38.4%	41.1%	43.8%	46.6%

Exh. DPS-PLW-2, Section II, pg. 1.

119. This is a calculation, derived from the cited findings.

120. This is a calculation, derived from the cited findings.

139. The current mean and median 2007 DSL penetration rates for comparable companies are approximately 13 percent. The high observed rate was 24.2 percent. King reb. pf. at 18; exh. WEK-1, table 4.6.

140. In 2008, FairPoint anticipates receiving approximately 25 percent of its revenues from DSL. Over time, DSL revenues will play an increasingly important role in FairPoint's financial success. Tr. 9/6/07 at 53 (Leach)(confidential).

141. Because DSL and broadband are emerging services, there is no historical basis for objectively determining whether FairPoint's projections to increase its DSL penetration rate is reasonable. King pf. at 18; tr. 9/6/07 at 218–219 (King).

142. Large cable companies offer so-called "triple-play" services which include voice, data and video. Tr. 9/20/07 at 167–168 (Nixon).

143. FairPoint claims that its past success in providing retail DSL services is among the best in the industry, and that its retail DSL penetration rates were as high as 24 percent in March 2007. Exh. WL-2, table 4.4; tr. 9/6/07 at 55 (Leach)(confidential).

144. Verizon's union contract, which FairPoint is assuming, includes a provision that requires union employees to install new technologies and network facilities. Wheaton pf. at 8.

145. FairPoint projects an increase of approximately 19,000 subscriber lines for toll services in the NNE operation over the planning horizon. Because of anticipated declining access lines, this increases the projected penetration rate by 21 percent, as follows:

Year	2008	2009	2010	2011	2012	2013	2014	2015
LDSubscribers (000)	632	642	651	651	651	651	651	651
Penetration of Retail Lines	54.0%	58.0%	62.0%	64.0%	67.0%	69.0%	71.0%	72.0%

Exh. DPS-PLW-2, Section II, pg. 1.

g. Projected Expenses

146. FairPoint has projected that approximately $65 to $75 million in "synergies" would be achieved in the first full year of operation. These synergies represent the difference between the allocated costs for functions performed by Verizon's subsidiaries outside of the NNE region and the incremental direct cost that FairPoint expects to incur to replace these functions. The primary

savings that FairPoint expects to realize include expenses that Verizon allocated to the NNE operations for shared assets, network and information technology, and customer services. The primary costs that FairPoint expects to incur to replace Verizon's allocated costs include functions related to engineering and operations, regulatory, buildings, and finance. Leach pf. reb. at 40–41; exh. DPS-PLW-2, Section III, pg. 1 (Confidential).

147. Attaining the projected synergies depends in part on a successful integration of Verizon's existing NNE operations into FairPoint's operational model, including the functionality of 600 Verizon systems and sub-systems into FairPoint's newly constructed operational support system. Haga/Kurtze pf. reb. at 21, Leach pf. reb. at 44–45.

148. FairPoint is committed, under its TSA with Verizon, to pay a significant fee after closing in each month that Verizon provides back office functions. The TSA fee schedule provides payments for four component services, as follows:

Schedule A — For "back-office" services, for the first 8 months after the closing date, FairPoint must pay $14.2 million per month. In months 9 through 12, the fee is reduced by $500,000 each month. In month 13, the fee increases to $14.7 million, and thereafter the fee will increase by $500,000 each month until termination of Schedule A services.

Schedule B — For isolation of information systems involving the cutover of back office and ISP services, FairPoint will pay $34.0 million. However, if isolation occurs within three months of the closing date, FairPoint will pay $41.5 million.

Schedule C — For employee benefits services, FairPoint will pay a fee of $52,000 per month.

Schedule D — For ISP services, FairPoint will pay a fee stated in a confidential schedule.

Smith pf. at 30.

149. FairPoint has projected TSA expenses of $100 million in 2008. No other transition expenses are anticipated beyond 2008. Leach reb. pf. at 21.

150. FairPoint anticipates the following operating expenses for its NNE operations during 2009 through 2015:

Year	2009	2010	2011	2012	2013	2014	2015

Operating Expense (M)	$709	$714	$721	$727	$734	$742	$748
Percent Change		0.8%	1.0%	0.8%	0.9%	1.1%	0.8%

Exh. DPS-PLW-2, Section I, pg. 2.

151. In 2009, FairPoint anticipates its direct labor cost as accounting for more than 55 percent of FairPoint's total LEC expenses. Exh. Labor-9 at 3 (confidential).

152. After 2008, FairPoint anticipates decreasing its total cost for salaries and wages paid every year. Exh. Labor-9; tr. 9/5/07 at 182 (Leach)(confidential).

153. As of September, 2007, Verizon Vermont's outside plant work force consisted of 175 splice service technicians and 47 outside plant technicians. Tr. 9/18/07 at 40 (Smee).

154. FairPoint anticipates hiring six more splice technicians initially in Vermont, and has budgeted for those additional positions. Tr. 9/17/07 at 218 (Smee); tr. 9/20/07 at 199–200 (Nixon).

155. FairPoint's financial projections assume that it can reduce current employee numbers by 4.0 to 4.5 percent annually. Exh. Labor-12; tr. 9/5/07 at 184 (Leach)(confidential).

156. A decrease in employee count by 4.0 or 4.5 percent per year is consistent with Verizon's recent experience. FairPoint discussed with Verizon whether Verizon has had special programs aimed at increasing employee attrition. However, FairPoint did not analyze this factor in detail, and it did not adjust its anticipated attrition rates for that factor. Exh. Labor-12; tr. 9/5/07 at 184 (Leach)(confidential).

h. Cash Flow Sensitivity

157. The Department conducted a sensitivity analysis using seven scenarios to test the sensitivity of FairPoint's financial capacity to changes in costs and revenues. These scenarios included increases in operating expenses, increases in capital expenditures, increases in interest rates, and reductions in revenues. Jeanson sur. pf. at 3.

158. In each scenario, the Department tested FairPoint's operations for a cash surplus or "cushion" against its two lender covenants. The analysis tested: (1) EBITDA Cushion;[121] and (2) Long-Term Debt Cushion.[122] Financial cushion represents the ability for FairPoint to absorb cost increases or revenue decreases due to unanticipated events or transactions or assumptions that prove to be inaccurate and still meet the needs of its various stakeholders. Jeanson sur. pf. at 6–7.

159. The base case in the analysis assumed that FairPoint's revenue would be decreased by $31 million per year due to expected regulatory adjustments in Vermont, Maine and New Hampshire. These adjustments are a reasonable starting point for the analysis. In the base case, FairPoint had the following amounts of financial cushion, in millions.

Year	2008	2009	2010	2011	2012	2013	2014	2015
EBITDA Cushion	$146	$170	$169	$149	$141	$129	$120	$110
Long-Term Debt Cushion	$213	$279	$341	$391	$430	$461	$472	$472

Jeanson reb. pf. at 5; exh. DPS-JFJ-2.

160. The Department's sensitivity analysis indicates that FairPoint has the financial capacity to absorb some unanti cipated cost increases. These included: (1) one-time conversion-related expenditures increased by $100 million in 2008; (2) capital expenditures increased $50 million each year above base case, beginning in 2008; (3) operating expenditures increased $50 million each year above base case, beginning in 2008; and (4) interest rates increased by 200 basis points. Jeanson sur. pf. at 8–11.

161. If revenues were five percent lower each year than base case, beginning in 2008, then FairPoint would be required to reduce dividends in 2011. In 2012 and later, the deficiency in Long-Term Debt Cushion would be substantially greater than FairPoint's planned dividend payouts. Jeanson sur. pf. at 10.

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121. EBITDA Cushion represents the amount by which operating expenses can increase or revenues decrease (or some combination of the two) and still satisfy the debt coverage ratio specified in the debt covenants. This coverage ratio is defined as Adjusted EBITDA divided by Interest Expense, and must exceed 2.0.

122. Long-term Debt Cushion represents the amount of additional borrowing capacity available to FairPoint while satisfying the debt coverage ratio defined as Net Long-term Debt divided by Adjusted EBITDA. This coverage ratio must be not exceed 5.75 in 2008 and must not exceed 5.50 each year thereafter.

162. If capital expenditures and operating expenditures each were $50 million higher each year than base case, beginning in 2008, FairPoint would be required to reduce dividends in 2011 and later. In 2012 and later, the deficiency in Long-Term Debt Cushion would be substantially greater than FairPoint's planned dividend payouts. This scenario is not considered likely. Jeanson sur. pf. at 3, 11.

163. The Department also considered a "perfect storm" scenario. In this scenario, (a) capital expenditures increase by $50 million per year, (b) operating expenses increase by $75 million per year, (c) conversion-related capital expenditures increase by $50 million, (d) operating revenues are less by two percent each year, and (e) the interest rate on borrowings increases by 100 basis points. The results are that even with the elimination of the cash dividend paid to common shareholders, FairPoint would not be in compliance with the Net Long-term Debt coverage ratio beginning in 2008. This scenario is not considered likely. Jeanson sur. pf. at 3, 11.

164. It is reasonable to expect that at some time during the forecast period that FairPoint will have to reduce dividend payments for one or more years in order to remain in compliance with its debt coverage ratios. Jeanson sur. pf. at 3.

i. Incentive Regulation Plan

165. Verizon's rates in Vermont are based on its Incentive Regulation Plan. FairPoint proposes to assume Verizon Vermont's rights and obligations under its current Incentive Regulation Plan, which expires in 2010. Nixon pf. at 25.

166. Rates under the current Plan were originally set based on a traditional cost of service/revenue requirement consisting of earning a rate of return on net book value, taxes and operating expenses. Wheaton pf. at 12–13. Behrns sur. pf. at 4–7.

167. The Board has generally required carriers seeking renewal or extension of an alternative regulation plan to file a complete cost of service analysis, including an analysis of net plant in service. The Board requires this because without such an assessment, the Board could not determine whether rates would be lower under the Incentive Regulation Plan and could therefore not make a finding of public good necessary to approve a Plan. Behrns sur. pf. at 7; *Investigation*

into a Successor Incentive Regulation Plan for Verizon New England Inc., d/b/a Verizon Vermont, Docket 6959, Order of 9/26/05 at 6.

168. FairPoint's financial projections assume that existing rates will continue indefinitely over its eight-year planning period through 2015. FairPoint did not consider the possibility of an intervening rate adjustment based on a required traditional cost-of-service filing. FairPoint also did not consider the possibility that the Plan might not be extended in 2010 and that its rates could become subject to traditional cost-of-service ratemaking. Behrns sur. pf. at 4-7; tr. 9/6/07 at 173 and 180 (King) ; tr. 9/7/07 at 117 (Balhoff); tr. 9/5/07 at 37–38 (Leach).

169. If the Board were to reduce rates based on FairPoint's costs, the company might have to reduce dividends. Tr. 9/6/07 at 140 (Leach).

170. In 2010 when the Board considers whether to extend the Incentive Regulation Plan, FairPoint's expenditures will likely be below the level currently built into rates. Behrns sur. pf. at 12.

171. In 2010 when the Board considers whether to extend the Incentive Regulation Plan, FairPoint's cost of capital may be substantially less than Verizon's present cost of capital, largely because FairPoint plans for more debt. Behrns sur. pf. at 12.

172. In 2010 when the Board considers whether to extend the Incentive Regulation Plan, FairPoint's net plant value is likely to be lower than the level currently built into Plan rates. Leach reb. pf. at 46–47; tr. 9/5/07 at 137–138 (Leach).

173. As the result of a stipulation leading to the current Incentive Regulation Plan, Verizon's rates are approximately $11.24 million per year above its costs of service, defined by traditional ratemaking methods. *Investigation into a Successor Incentive Regulation Plan for Verizon New England Inc., d/b/a Verizon Vermont*, Dockets 6959/7142, Order of 4/27/06 at 2–3, 21 (approving stipulation that voided three planned rate decreases).

3. Discussion

A regulated utility proposing a merger must establish that the surviving company will be financially sound. The company must show that it has the financial ability to maintain service quality and make suitable improvements to its plant, while at the same time satisfying its financial obligations.

Normally, we look first at a utility's projections of net earnings after dividends, or the trend in shareholder equity. Where a utility has plausibly projected a positive or even a neutral trend on shareholder equity, we generally find that the company is financially sound. Here, however, FairPoint does not even attempt to satisfy that traditional test. Instead, FairPoint candidly admits that it plans in every year within its planning horizon of 2015 to distribute dividends significantly in excess of its book earnings.

Supported by at least one Department witness, FairPoint asserts that, today, "cash is king." The company argues that the Board should not use traditional accounting concepts such as shareholder equity and net income to assess financial soundness. Instead, FairPoint maintains that the Board should look solely to its ability to generate positive cash flows and rely on its projected free cash "cushion" of approximately $70 million per year as sufficient insurance against unforeseen financial difficulties.

For present purposes, we accept that cash flow is currently the relevant criterion for the financial community. However, as utility regulators, we should take a different, and more cautious, view. Banks and other lenders have a right to be repaid even when a company's shareholders do not earn dividends. Banks therefore can rationally ignore, or weigh lightly, some risks that are important to ratepayers and perhaps even some that are important to shareholders.

FairPoint argues that the interest of its creditors and customers are aligned because its existing debt covenants would require FairPoint to suspend dividends in the event of unforeseen financial pressures.[123] While we accept that such an alignment can exist, there are important exceptions.

From a ratepayer's perspective, reliable high-quality service is of great importance. A company that is short of cash can find many ways to cut corners that will eventually harm service but that produce a temporary improvement in the company's cash position. These include eliminating outside plant and back-office employees and deferring capital expenditures and maintenance. This is especially worrisome with regard to outside plant work (such as removing

123. Leach reb. pf. at 64.

double poles and line clearing) that does not immediately affect network performance. Succumbing to such temptations can compromise ratepayers' interests, but without apparently jeopardizing lender interests.[124] Of particular interest at the moment, management of a cash-short enterprise could defer investments aimed at increasing broadband deployment. A few years of neglect of this sort could create problems with the plant and workforce that would take years to repair. In addition, although we do not think the risk of bankruptcy is high, any such event of bankruptcy would be likely to postpone new investment in Vermont's network for years.

The different interests of lenders and ratepayers is illustrated by FairPoint's lending covenants. FairPoint has accepted two covenants. The first sets an upper limit on the ratio of debt to EBITDA. The second sets a lower limit on the ratio of EBITDA to interest payments. Both covenants are designed to prevent FairPoint from borrowing excessively. In both cases, the relevant ratio can be improved by increasing EBITDA. In turn, EBITDA can be improved by reducing cash outlays for capital or operating expense.

FairPoint plans to issue $142 million in dividends each year to shareholders. It maintains that these dividends are not sacrosanct and can be a secondary buffer against unanticipated financial difficulty. FairPoint represents that it would cut dividends if necessary to maintain quality service and act primarily to protect its relationship with customers, employees and the communities it serves.[125]

We accept the sincerity of FairPoint's statements that dividends will be treated as optional if there is a cash shortage. But a future cash shortage would present FairPoint's management with other options as well, some of which might be more congenial at the time. FairPoint's stock is not investment grade, and it projects further declines in shareholder equity. Therefore FairPoint will be able to attract equity investors only with consistent dividends. Indeed, Standard & Poor's has characterized FairPoint's "shareholder-oriented financial policy" and its high dividend rate policy as a weakness. Moreover, FairPoint has a history of frequent

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124. Some might even be perceived by lenders as favorable. For example, eliminating employee positions will improve EBITDA. FairPoint's two lender covenants both are improved by larger EBITDA. For example, the debt coverage ratio is defined as Adjusted EBITDA divided by Interest Expense, and it must exceed 2.25. Increasing EBITDA increases the ratio and reduces the risk of noncompliance.

125. *E.g.,* Leach reb. pf. at 57–58.

acquisitions, and this suggests that FairPoint may be reluctant in the future to lose access to equity capital, even for a short period.

Therefore, if FairPoint's free cash flow, after dividends, should become negative in the future, we are concerned that FairPoint may be tempted to cut corners in ways other than by reducing dividends. For these reasons, we are reluctant to rely on voluntary dividend reductions as insurance against inadequate funding for capital and operating needs.

In the following subsections, we analyze the reasonableness of FairPoint's projections and, in so doing, examine the adequacy of FairPoint's postulated cash cushion. For purposes of this evaluation, we accept FairPoint's invitation to analyze the financial soundness criterion primarily based on its free cash flow. We also accept that $70 million per year is a significant cushion of free cash. However, for the reasons explained above, the reliability of this cushion is critical for us to conclude that FairPoint is financially sound. Given the significant risks to ratepayers, we used conservative but still plausible assumptions. First we consider the uncertainty in FairPoint's revenue projections.

a. Revenue

i. Line Losses

FairPoint's largest source of revenue will be its switched access lines. FairPoint assumes that it will lose 6.2% of its lines in the first year, consistent with Verizon's current rate of loss. Thereafter, FairPoint projects smaller losses each year, eventually tailing off to 2.3% per year. FairPoint argues this projection is consistent with historical trends in the telecommunications industry and historical experience in the region.

FairPoint views itself as a highly competitive carrier experienced in serving rural areas with advanced services. FairPoint also expects to offer a more competitive set of services that it believes will slow the rate of line loss.[126] We accept FairPoint's representations on this point. We are impressed with, and accept as accurate, FairPoint's stated intention and competency to provide excellent service.

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126. Leach pf. at 22, 24–25; King reb. pf. at 19; Balhoff pf. at 18–19.

Nevertheless, we conclude, for several reasons, that FairPoint's line loss projection may be unduly optimistic. Verizon's rate of loss increased from 4.8 percent in 2004 to 6.3 percent in 2006. Some of these recent losses may be due to Verizon's behavior, but certainly not all. There are larger forces at work in the telecommunications industry, such as migration to wireless, elimination of second switched lines to residences and competition from broadband-based services. The record shows an increasing rate of line loss in the recent past, and FairPoint's plans to reduce a loss rate that is increasing every year are not consistent with historical trends. FairPoint simply contends that it will be able to decrease the rate of loss by offering more competitive services. However, this seems optimistic and inconsistent with historical trends toward ever increasing line loss rates. FairPoint has not persuaded us that competency and good intentions can stabilize, much less reverse, these trends.

Even more important, the combination of widespread broadband and the Internet offers a new alternative to switched access lines. Customers with broadband access can easily acquire a fully functioning telephone service independent of the incumbent local exchange carrier. While these "VoIP" customers today are only a small share of the existing switched access line market, that share is growing.

Cable providers such as Comcast are now for the first time offering proprietary VoIP services on their existing cable systems in Vermont.[127] We view this as a significant development for the incumbent local exchange industry. Customers who may have been tempted to acquire VoIP service in the past will now be able to buy the service from a known carrier with whom they have a regular billing and payment relationship. Moreover, the service may be better than other VoIP services that ride the public Internet. Cable television companies already have direct connections to most customers, and they have additional opportunities for quality control. Moreover, where a customer already has digital video available, the company can add VoIP services at a low incremental cost. This gives cable providers the opportunity to bundle voice service with high-speed internet and video programming services. We conclude that the arrival

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127. We have no reason to believe that the rest of northern New England will have a substantially different experience. However, we do know that Portland, Maine has had cable-based competition for several years, and is an exception. *See* tr. 9/7/07 at 144 (Balhoff).

of cable-based VoIP service has a significant chance of exacerbating the existing trends in access line losses by incumbent telephone companies. The record indicates that cable can be expected to achieve a market share somewhere between 25 and 40 percent, with the most common estimate at 30 percent.

We have examined the record to test whether the downward plausible uncertainties in FairPoint's forecast are larger than its cash cushion. FairPoint constructed a computerized financial model and made that model available to the parties, but it is not in the record and is therefore not available to us. Accordingly, we are not able to evaluate fully how a given change to underlying revenue or expense assumptions would affect FairPoint's net income or cash position. Instead, we developed two specific, less optimistic, scenarios for access line losses, and then estimated the lost revenues in comparison to FairPoint's base case.[128]

First, we considered a "Steady State Scenario" under which FairPoint would continue to lose lines at exactly six percent per year. This scenario represents a middle ground between current trends, in which line losses are increasing each year, and FairPoint's projections, in which line losses would be smaller each year. As one might expect, the line loss differences are small at first, but by 2015, the difference is substantial, 164,000 lines.

To estimate the revenue effects[129] of the Steady State Scenario, we applied a constant figure for average revenue per switched access line, $730 per line per year.[130] The results are proportional to line counts, and larger revenue losses appear in the later years. The overall result

128. These scenarios take the testimony presented by FairPoint during hearing and adjust a single assumption included in FairPoint's projections — the rate of line losses. The scenarios do not represent new models or a reworking of the evidence that was presented at hearing.

129. We recognize that if access lines do indeed reduce more rapidly than anticipated, there would be some compensating effects on operating expenses and taxes. In particular, if line losses are greater than FairPoint estimates, it is reasonable to conclude that FairPoint may be able to reduce its workforce and operating costs somewhat. Because we do not have FairPoint's computer model in the record, we do not model those offsetting factors here. Nevertheless, we conclude that the revenue loss calculation is useful for estimating the order of magnitude of the possible errors in FairPoint's projections. Moreover, the effect of the decrease in operating expenses that we have not calculated will be at least partially offset by the fact that we have used conservative assumptions for line losses and revenue declines.

130. This number is based on historical Verizon data. FairPoint's financial plan anticipated significantly increasing its average revenue per access line over the planning horizon. However, the details of those projections were filed under a claim of confidentiality. By using the historical Verizon revenue figure, we consciously err on the side of under-estimating the revenue loss.

of the Steady State Scenario is consistent with FairPoint's assertions, at least through 2011. In these early years at least, revenue losses are smaller than the $70 million "cushion" planned by FairPoint.

Our second scenario was adjusted for what appears to be the likely effects of cable VoIP. We understand that cable VoIP may acquire a 25 to 40 percent market share eventually. However, we assumed significantly smaller access line reductions in our "VoIP Scenario." We wanted to give FairPoint the benefit of some doubt that its marketing will be more effective than Verizon's. In addition, we assumed that some switched access customers have already shifted their service to Internet-based VoIP services such as Vonage. Removing a full 30 percent of FairPoint's access lines would double-count those customers. We used a much more modest estimate in which VoIP would cause incremental five percent line losses in 2009 and again in 2010.

The VoIP Scenario makes a significant difference. Under FairPoint's base case, in 2015 FairPoint would have 1,015,000 lines. Under the VoIP Scenario, FairPoint would have only 763,000 lines in 2015. The revenue change is also significant. By 2015, FairPoint would have 22 percent less switched access revenue than in the base case.

The VoIP Scenario also makes a significant financial difference in the early years. In 2009, FairPoint's revenues would fall $54 million short of its projections. This approaches but does not reach the amount of FairPoint's cushion. Beginning in 2010, however, FairPoint's revenues under the VoIP Scenario would fall short by $106 million. Even before consideration of other risks discussed below, this switched line reduction would, by itself, completely eliminate the $70 million cushion and require a significant cut in FairPoint's dividends.

For these reasons, we conclude that FairPoint's projections regarding switched line losses in the NNE region are optimistic, and under reasonably foreseeable circumstances, might force FairPoint to decide whether to reduce dividends or reduce capital or operating expenses.

ii. DSL Revenue

FairPoint projects that it will increase its DSL penetration rate from 23.8 percent to 46.6 percent by 2015. Much of this will come from increasing the number of customers who can purchase DSL. A good deal, however, comes from FairPoint's assumption that an increasing share of customers who can purchase DSL *will* purchase DSL. FairPoint relies on its past experience in providing such services in the existing FairPoint service territories. FairPoint claims that it has proven that it is better at providing the high speed data availability to its customers, and getting more customers to take it than any other sizeable company in the industry.[131]

FairPoint may indeed be the best in class among comparable service providers. However, its projections require it to achieve penetration rates substantially higher in 2015 than any carrier currently in FairPoint's comparison group has yet achieved. This may be reasonable because, as FairPoint asserts, broadband is a relatively new service, and more customers are purchasing it over time. However, FairPoint acknowledges that there exists no historical basis for objectively determining whether its projection of a 46 percent DSL subscribership rate is reasonable. Indeed, FairPoint's witness King candidly admitted that gauging the reasonableness of FairPoint's penetration assumptions "is a subjective assessment dependent on one's view of the overall acceptance of broadband."[132] While FairPoint may actually achieve this penetration rate, we conclude that the projection has substantial uncertainty associated with it.

Also, FairPoint has not adequately shown that it has considered the effects of cable modem competition. The cable industry has been first-to-market in many areas, and it has offered innovative pricing. The cable industry is now a significant competitor in high-speed Internet access. FairPoint asserts that it does best selling DSL in rural areas. Also, if FairPoint were to be the first to deploy, it might hope to achieve a high market share of customers who take broadband. But cable modems have now been offered in Vermont (and, we assume, the other

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131. FairPoint's DSL analysis raises a different concern. We were surprised to discover that FairPoint appears to have projected operating losses for its ISP operations every year, and that those losses are expected to increase over time. The parties did not litigate this issue, and we may misunderstand the exhibit on which we based this observation. Nevertheless, we understood FairPoint to assert that such data operations will be the central feature of future telecommunications networks, and we assumed that the price paid to Verizon had included a premium over book value largely because of the financial potential of this line of business. This expectation appears to conflict with the financial model showing that the operating losses grow over time. If FairPoint makes further filings in this docket seeking approval of the proposed transaction, those filings should clarify this issue.

132. King reb. pf. at 18.

two states) for years. Verizon missed the opportunity to be first-to-market some years ago, and it seems doubtful that FairPoint can recover as much lost ground as it anticipates.

We are also concerned about capitalization. Even in the absence of cable competition, to substantially increase DSL subscribership levels in the three northern New England states would be a significant challenge even for a well-capitalized company. We are concerned that because FairPoint relies heavily on debt, and because it projects reducing shareholder equity each year, it may not be able to make the necessary capital investments soon enough to achieve its projected broadband revenues.

Finally, FairPoint's ability to deploy retail DSL services depends on a labor force with the appropriate qualifications. FairPoint is assuming Verizon's union contract, which requires union employees to install new technologies and network facilities. FairPoint is uncertain about the number of qualified technicians who will transfer to FairPoint at closing, and there is a significant possibility that not enough union technicians will remain in Vermont. This is an additional risk factor for FairPoint's planned DSL revenues.

For these reasons, we conclude that FairPoint's projections regarding DSL penetration and DSL revenue in the NNE region are optimistic, and under reasonably foreseeable circumstances, might force FairPoint to decide whether to reduce dividends or reduce capital or operating expenses.

iii. Toll Revenue

FairPoint anticipates substantially increasing the percentage of its customers taking its own toll service. The percentage is projected to increase by 2015 from 54% in 2008 to 72% in 2015.

We are not satisfied that this is likely to occur. Some percentage increase may indeed be likely as more customers purchase "bundled" services that include both local and toll services. However, FairPoint also anticipates an absolute increase in the number of its toll subscribers, from 632,000 in 2008 to 651,000 in 2015. This would be a 3 percent increase in toll customers at the same time that FairPoint is projecting a 23 percent loss in access lines. While we understand that major changes are occurring in the telecommunications industry, we are not persuaded that FairPoint is likely to experience an increase in toll subscribers while it loses tens of thousands of access lines. This is particularly questionable when the main new sources of competition — wireless and cable VoIP — offer competing services that usually include an unlimited calling option.

For these reasons, we conclude that FairPoint's projections regarding toll penetration and toll revenue in the NNE region are optimistic, and under reasonably foreseeable circumstances, might force FairPoint to decide whether to reduce dividends or reduce capital or operating expenses.

b. Expenses

FairPoint projects significant operating expense savings both initially and over time.

i. Short-Term Savings

FairPoint estimates its initial savings, which it has called "synergies," at $65 million per year. The estimate is based on replacing Verizon's out-of-region functions with in-region services at lower costs. FairPoint claims that this is possible because it would be starting with a "clean sheet" and could operate well below Verizon's allocated costs.[133]

This estimate has significant uncertainty. FairPoint may not be able to achieve all of its projected savings within one year of closing. In addition, FairPoint's projected cost saving may not match the final cost. Financial success as measured by free cash flows therefore presupposes operational success in transferring to FairPoint's planned new back-office systems and in deriving large savings relative to Verizon's costs of providing the same services. As we discuss in more detail below, this will require transferring the data and functionality of more than 600 Verizon information systems to FairPoint's newer but different systems.

FairPoint anticipates a system cutover in May of 2008, only five months after closing. If the integration of these systems were delayed or disrupted, FairPoint could have to pay concurrently for its own new systems and new employees while at the same time paying Verizon for extended services under the TSA. Payments under that agreement are significant, and would

133. Leach pf. reb. at 41.

never be less than $12.2 million per month. Moreover, the payments would increase substantially 12 months after closing, by one-half million dollars per month. Therefore, if cutover were delayed by even one month, it would have a significant financial effect on FairPoint. A six-month delay in cutover, while unlikely, would cost FairPoint an amount of money approximately equal to its projected annual cash flow cushion.

In another section we examine in detail FairPoint's transition plans and explain our view of its likely success. In summary, while we recognize that the transition undertaking is very complex and creates substantial risks, we are satisifed with FairPoint's preparations for that transition and we think it is reasonably likely to succeed without substantial delays. For that reason, we conclude here that FairPoint's estimated initial estimate for expense savings appears reasonable, even though any delays, however unlikely, could severely impair FairPoint's projected cash flow.

ii. Long-Term Savings

From 2009 onward, FairPoint projects operating expense increases for its northern New England operations of about 1 percent per year. As with any telephone company, a major part of FairPoint's operating expenses will be employee expense. FairPoint also anticipates that its employee expense will decline every year after 2008. To accomplish this, FairPoint anticipates reducing the number of employees annually by 4.0 to 4.5 percent per year over the planning horizon.

This estimate is consistent with Verizon's recent experience. However, the record is unclear about the extent to which Verizon's recent experience with attrition is based on special retirement inducements. FairPoint did not adjust for this variable, but the record does not show that FairPoint examined the issue carefully. As a result, if FairPoint relies solely on voluntary attrition to reduce its work force, it may have more employees than it has projected.

More important, FairPoint's planned work force may not be adequate to maintain service. FairPoint does anticipate hiring a few more splicers initially to deal with the outside plant work backlog. Also, we accept FairPoint's argument that line losses can justify reducing a company's work force. However, it appears that FairPoint's projected attrition rate of 4 to 4.5 percent annually actually exceeds its annual line loss rate of 3.6 percent. Since FairPoint will have to maintain its existing outside plant and central office equipment even as its line counts shrink, and will need to keep employees for this purpose, we would expect that its rate of workforce reduction would be less than, not greater than, the pace of line losses. A more likely scenario would be an employee attrition rate lower than the line loss rate unless FairPoint chooses to allow a degradation of service quality.

In addition, FairPoint's attrition projections seem implausible in light of what we have learned about the state of Verizon's work force and its network. The record shows that over many years Verizon has allowed a backlog of pole work to accumulate.[134] We doubt that FairPoint will be able to eliminate that backlog, keep up with new work, and reduce its work force by 4.0 to 4.5 percent per year. While FairPoint management would have discretion to try this strategy, we believe it would be more than likely to produce unacceptable results.

In sum, our review of the record does not persuade us that we should rely upon FairPoint's forecasted employee wages and benefits. For this reason, we conclude that FairPoint's projections regarding future operating expense in the NNE region are optimistic, and under reasonably foreseeable circumstances, might force FairPoint to decide whether to reduce dividends or reduce capital or operating expenses.

c. Future Rates

FairPoint proposes to assume Verizon's current rates, which were set under an Incentive Regulation Plan. That Plan expires at the end of 2010. Historically, when Verizon's rates have been set or adjusted in an alternative regulation plan, the Board has first conducted a rate-of-

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134. There is nothing in the record suggesting that Verizon recently increased its workforce. On the contrary, a response to a Board data request showed that Verizon has reduced its Vermont labor force from 430 in 2000 to 308 in 2006. Verizon response to Board data request.

return analysis to see if rate adjustments are needed.[135] That analysis includes consideration of the utility's net plant in service, cost of capital, and operating expense.

We cannot now determine what rate levels will be reasonable in 2010. However, the record suggests several independent reasons to believe that a substantial rate adjustment may be appropriate at that time.[136] First, a downward rate adjustment would be likely even if FairPoint were to present exactly the same underlying facts that Verizon presented in its last Incentive Regulation Plan case, because Verizon's current rates currently include $11 million of annual revenue that Verizon was allowed to keep in return for building broadband. Second, assuming the accuracy of FairPoint's projections for capital and expenses, FairPoint's net plant value and operating expenses will be lower by 2010. An additional downward pressure on FairPoint's rates arises if FairPoint actually derives cost savings from the new systems relative to Verizon. Typically, the Board and other regulator agencies pass these merger synergies on to ratepayers.

A cost-of-service analysis in 2010 could also have a positive side for FairPoint, giving it (or Verizon if the proposed transaction does not close) an opportunity to address some financial problems. For example, if FairPoint's line losses turn out to be worse than it projected, FairPoint might seek higher rates in 2010. While this offers the possibility of ameliorating any post-2010 financial harm that FairPoint has not anticipated, the price would be higher consumer rates in a way that also is not currently anticipated. This possibility of higher rates may increase

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135. The Board has given three reasons:

First, a review is necessary to determine whether the utilities rates are just and reasonable at the outset of the Plan. If during the Plan, a utility is able to increase earnings, such earnings must stem from management's decisions, and not from artificially high initial rates.

Second, only when the Board determines that incentive regulation promotes the public good can a plan be adopted. Making such a determination requires a comparative analysis of the merits of both a plan and traditional regulation. The analysis examines the level of customer benefits under both regulatory regimes. The primary question that the Board seeks to answer is: whether rates and customer value would be higher or lower if a proposed incentive regulation plan is approved.

Third, a cost-of-service review provides the Board with a meaningful measurement tool to fully assess a utility's ability to satisfying its commitments to maintain service quality and deploy broadband services. If, for example, a company failed to satisfy broadband commitments made in a plan, a cost-of-service review might provide information on whether the cause was competition that seriously eroded the company's financial capacity or mere negligence by the carrier. Docket 6959, Order of 9/26/05 at 23–24.

136. The probability of these adjustments is independent of whether FairPoint actually continues under an Plan after 2010, because if it does not, it will revert to rate-of-return regulation.

FairPoint's ultimate chance of financial success, but it does little to persuade us that the Proposed Transaction should be approved.

In sum, FairPoint's planning assumption about revenues appears to be inconsistent with Vermont's current ratemaking practices and policy, including those associated with the renewal of alternative regulation plans. As a consequence, FairPoint appears not to have fully considered the potential implications of a traditional cost-of-service review, nor the effect of such a review on the company's current free cash flow. On balance, while there is some possibility that such a review would increase rates, the assumptions made by FairPoint's cash flow analysis seem internally inconsistent, and are more likely than not to overstate actual cash flow.

For these reasons, we conclude that FairPoint's projections regarding post-2010 rates in Vermont are optimistic, and under reasonably foreseeable circumstances, might force FairPoint to decide whether to reduce dividends or reduce capital or operating expenses.

d. Cash Flow Sensitivity Analysis

In the preceding sections, we examined the several uncertainties in FairPoint's projections of revenues and expenses. We found significant risks in switched access line revenues, DSL revenues, toll revenues, expenses, and future rate reductions. We do not have in the record FairPoint's computer model for its projections. Therefore even if we were to alter FairPoint's assumptions, we could not perform a definitive cash flow calculation.

However, the Department's sensitivity analysis suggests how much these uncertainties could affect financial soundness. The Department's witness Jeanson varied FairPoint's assumptions in several ways to determine whether the existing debt covenants would require FairPoint to reduce its dividends. In some cases he found that FairPoint could satisfy lenders by reducing dividends. In other scenarios losses were larger, and FairPoint seemed likely to violate its existing debt covenants. Some of the most alarming scenarios were judged as unlikely to occur, even by the Department's witness. However, one of the other scenarios is particularly helpful here because it makes assumptions about revenue loss that seem well within the range of FairPoint's plausible futures.

In one scenario, Mr. Jeanson assumed revenues five percent below the base case in every year. He concluded that FairPoint would have to reduce its dividends in 2011 and it would be unable to make debt payments in 2012. Given the several weaknesses in FairPoint's revenue projections, we think there is a substantial possibility of a revenue shortages of at least this size. In particular, given our concern about voice competition from cable companies, we think a cash flow difference of more than minus five percent could occur in 2009 or 2010. This would require FairPoint to choose between dividend restrictions and tactics that improve EBITDA.

e. Conclusion

FairPoint's financial soundness rises or falls solely on its ability to generate sufficient cash flow. However, FairPoint's financial projections are optimistic in several ways, and fail to recognize material uncertainties. The projections are optimistic regarding the loss of access lines; under a plausible scenario, FairPoint could fully exhaust its $70 million free cash "cushion" in 2010. The projections are also optimistic regarding DSL revenues, toll revenues, expenditure management, and post-2010 rate levels.

Our own analysis shows that reasonably foreseeable access line losses could force FairPoint to reduce dividends. The Jeanson analysis confirms that unplanned but foreseeable changes in revenues and operating expense can force FairPoint to reduce dividends. The Jeanson analysis also shows that under at least one foreseeable scenario (a five percent revenue reduction), FairPoint could fail to meet its debt obligations by 2012.

To realize its expectations, FairPoint would need to do several things very well. It would need to successfully integrate the northern New England operations into FairPoint's existing businesses without a major interruption in customer services. It would need to slow the currently accelerating loss of access lines. It would need to substantially increase its penetration rate for DSL to currently unprecedented levels. It would need to substantially increase its penetration rate for toll services. It would need to aggressively manage its operating expenses, reducing its workforce below the level it would inherit from Verizon, but without harming service quality.

If everything goes well, FairPoint's financial plan can succeed. However, FairPoint would need to do virtually everything right. One major failure, or the concurrence of several partial failures, could leave FairPoint with a forced choice between reducing dividends and reducing necessary capital and operational spending. Even worse, there is a foreseeable risk of insolvency in 2012 or thereafter. Because we view these as foreseeable circumstances, we are not persuaded that FairPoint, if it closes as the transaction is currently structured, satisfies the financial soundness test.

f. Subsequent Consideration

In other parts of this Order, we conclude that the transaction would offer significant benefits to Vermonters. For that reason, we are willing to consider modifications to the currently Proposed Transaction that would leave FairPoint financially sound.

FairPoint and Verizon might address the problem in several ways or through a combination of adjustments and conditions to protect ratepayers. One obvious possibility would be to reduce the price paid to Verizon. Another possibility would be to reduce dividends planned for shareholders. Both of these actions would increase FairPoint's free cash flow and might even produce increases in shareholder equity over time.

FairPoint and Verizon might also propose financial mechanisms that would be useful in the event of a looming financial failure. While we do not believe such mechanisms would allow us to approve an acquisition by a fundamentally unsound company, they could substantially reduce ratepayer risk. One such mechanism might be to make some reserve funds available in the event of specific warning signs such as increasing trouble report rates, increasingly frequent or long service outages, or obviously falling behind on outside plant maintenance and construction. We were encouraged that FairPoint has already offered to use some of FairPoint's existing line of credit.[137] We were also encouraged by FairPoint's specific offer to suspend dividends if FairPoint does not meet capital spending targets in Vermont.[138]

In its proposed conditions numbered 4 through 7, the Department proposed several mechanisms to ensure that FairPoint's financial condition is carefully monitored and that,

137. Tr. 9/20/07 at 212 (Nixon); Leach reb. pf. at 64–65.

138. *E.g.,* Leach reb. pf. at 65 (offering reasonable annual capital expenditures "until the Board has evidence the performance criteria have been met").

assuming timely action by regulators, would protect ratepayers. Although we do not find FairPoint to be financially sound under the current proposed transaction, in any subsequent reconsideration involving different facts, we would accept the Department's recommendations in number 4, and we would impose the following condition in approving the merger:

> **FairPoint shall form a separate legal entity within the State of Vermont to separate all Vermont related assets and liabilities, if any, from the assets and liabilities of other FairPoint regulated, non-regulated and classic operations.**

In its proposed conditions numbered 5 though 7, the Department proposed a series of reporting and accounting rules and raised the possibility that in the future the Board might, by order, suspend a cash transfer from the Vermont operating company to the FairPoint parent corporation. In addition, the Department proposed that major contracts between FairPoint and its operating company in Vermont be negotiated at arms length While these safeguards would reduce ratepayer risk and increase the Board's ability to act in the event of impending financial failure by FairPoint, they are not the only possible way to approach the issue of adequate capital and operational spending in Vermont. Since we are inviting FairPoint to submit a revised financial proposal, we reserve for future consideration whether approval of a proposed merger should be conditioned in the way that the Department currently recommends.

Regardless of the approach ultimately adopted by the parties, however, FairPoint will still carry the burden of persuading us that acquiring lines in Vermont will leave it financially sound, both in the next few years and after 2010 when some pre-closing or post-closing events might lead to alterations of existing rates. Fundamentally, FairPoint must persuade us that its Vermont operations will have sufficient cash to invest in plant and to maintain satisfactory operations. Ultimately, this will require FairPoint to develop financial projections that acknowledge all significant and reasonably foreseeable financial risks.

D. FairPoint as a fair partner in business transactions

1. Just and reasonable terms and conditions

a. Findings

174. FairPoint has agreed to adopt all Verizon retail service obligations in Vermont. FairPoint will file tariffs matching current tariffs for Verizon Vermont with the same rates, terms and conditions at closing. In addition, FairPoint proposes to adopt virtually all of Verizon's access tariff and wholesale service requirements. Skrivan reb. pf. at 6; Nixon pf. at 26–27; Lafferty pf. at 18; Lafferty reb. pf. at 31.

175. Wholesale customers should continue to receive the services they receive today under the same rates, terms and conditions. Leach pf. at 6.

176. FairPoint will continue the existing arrangements with independent incumbent local exchange carriers with no change in rates, terms or conditions of the services that Verizon currently provides. Tr. 9/19/07 at 214–216 (Nixon); tr. 9/5/07 at 18–19 (Leach); exh. ITC-1 and ITC-2.

177. No existing Verizon retail service will be discontinued or interrupted as a result of the transaction. Nixon pf. at 27.

178. Verizon currently operates under an alterative regulation plan in Vermont which replaces rate-of-return regulation through 2010. FairPoint proposes to assume Verizon's rights and obligations under the terms of the Incentive Regulation Plan, including its obligations under the 2005–2010 Amended Retail Service Quality Plan ("SQ Plan").[139] Nixon pf. at 25–27; Skrivan reb. pf. at 9.

179. The Board found that, in the context of the Incentive Regulation Plan, Verizon's rates were just and reasonable. However, absent the commitments by Verizon to deploy broadband to at least 80 percent of its customers no later than 2010, Verizon would have been required to implement rate reductions totaling $8.18 million beginning in 2005 with additional rate decreases due in 2007 and 2008. By 2008, the net effect of these rate reductions would have been $11.24 million annually. Docket 6959/7142, Order of 4/27/07 at 2; Docket 6959, Order of 9/26/05 at 105 and Appendix B at 6; Lafferty pf. at 19.

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139. The service quality and investment provisions of the Plan are discussed below in Parts V.C.2 and V.C.6.

180. By assuming the Incentive Regulation Plan, FairPoint will be subject to all the pricing and other limitations therein, including the prohibition against raising rates for existing services during the term of the Incentive Regulation Plan. This will help ensure that ratepayers do not see higher rates or less favorable terms of service as a result of the acquisition. Lafferty pf. at 19; Nixon pf. at 27.

181. FairPoint also has committed not to raise prices on non-regulated services (including DSL) for one year. Tr. 9/5/07 at 72–76 (Leach).

182. Through December 31, 2010 (the end of the Incentive Regulation Plan), FairPoint also will not withdraw or increase the price of any regulated intrastate service offered by Verizon under tariff as of the closing date of the transaction without approval of the Board. Campbell reb. pf. at 35.

183. FairPoint will prorate all volume pricing provided for in any tariff or other agreement so that the volume pricing terms exclude volume requirements from states outside of the acquired Vermont operations. Campbell reb. pf. at 35.[140]

184. In addition to maintaining existing services, FairPoint plans to offer customers an increased selection of competitively-priced communications services bundles, providing greater choice in the marketplace for communications services. Leach pf. at 7; Skrivan reb. pf. at 22; Nixon pf. at 27.

185. FairPoint also intends to introduce a branded wireless communications product, which would create an additional wireless competitor in Vermont, Maine and New Hampshire. Leach pf. at 13–14.

186. FairPoint also has committed to comply with service quality standards, consumer protection standards, and requirements set forth in the relevant Board Orders. Nixon pf. at 25, 27, 29; Skrivan reb. pf. at 7.

187. The merger is expected to create a range of benefits for both retail and wholesale customers, including: access for more customers to advanced telecommunications and information services such as broadband Internet; more locally-focused customer service; and

140. FairPoint has agreed to such proration. FairPoint Reply Brief at 15 and Attachment 1 at 7.

competitive pricing of new bundled service offerings tailored to the desires of retail customers in the three states. Leach pf. at 6.

188. The commitments in findings 174–186 should ensure customers receive the same services and at least the same prices as provided by Verizon. Lafferty pf. at 18.

i. Transaction Costs

189. FairPoint has committed that it will not seek to recover transaction expenses through its rates. FairPoint also will not request to include any acquisition premium or amortization thereof in a future rate-base or rate-of-return proceeding. Other types of costs relating to this transaction, such as due diligence, negotiation, and costs to obtain financing, will also not be passed on to customers through regulated rates. Skrivan reb. pf. at 20; Leach pf. at 35; tr. 9/20/07 at 116–118 (Nixon); Nixon pf. at 27.

190. FairPoint will not seek to recover, or pass through to its customers, the costs associated with its modifications to Verizon's operations and the establishment and implementation of its own systems, including costs incurred under the Capgemini agreement, from wholesale customers and pole/conduit licensees. Skrivan reb. pf. at 21.

191. Increased costs due to FairPoint's need to develop and transition to new systems currently supported by Verizon, or which are incurred as a result of reliance on Verizon under the Transition Services Agreement ("TSA"), should also not be recoverable from ratepayers in any future ratemaking proceeding. Campbell pf. at 16 and 47.

192. FairPoint plans to capitalize some costs and may request the Board to allow it to recover the capitalized costs of systems that replace systems currently used by Verizon in some future rate proceeding. Skrivan reb. pf. at 20; tr. 9/7/07 at 186–192, 207–213 (Skrivan); exh. FP Cross 3.

193. FairPoint plans to account for the costs incurred under the TSA as operating expense and will allocate the expenses based on the services provided. Skrivan reb. pf. at 21.

ii. Eligible Telecommunications Carrier ("ETC")

194. For some Vermont customers in Verizon's service territory, Verizon and its network are still the only option for receiving affordable, reliable telephone service. Campbell pf. at 44.

195. Verizon was designated by the Board as an ETC in Docket 5918, *In re: Designation of Eligible Telecommunications Carriers Under the Telecommunications Act of 1996* (*In re: RCC Atlantic, Inc. d/b/a Unicel*), Order dated 12/5/02 at 6.

196. Verizon is presently the only wireline ETC in its territory. Campbell pf. at 44–45.

197. FairPoint intends to provide all of the services necessary to qualify as an ETC under the Federal Communications Act. Nixon pf. at 30.

198. FairPoint has requested a waiver of the "All-or-Nothing" rule from the Federal Communications Commission so that its existing, rate-of-return entities may continue to be regulated on a rate-of-return basis while FairPoint operates the acquired Verizon exchanges under price cap regulation. Nixon pf. at 31.

iii. Treatment of FairPoint's Existing Vermont Subsidiary

199. FairPoint Vermont is a separate subsidiary of FairPoint that owns and operates exchanges in Vermont under a separate Certificate of Public Good from the Board that it will continue to operate after the closing. Skrivan reb. pf. at 12.

200. If the Proposed Transaction is approved, FairPoint Vermont will be controlled by the same corporate parent as the entity comprising the newly-acquired Verizon territory. Campbell pf. at 42.

201. As a result of the Proposed Transaction, FairPoint would control more than ten percent of the subscriber lines installed in Vermont. Campbell pf. at 42.

202. FairPoint Vermont's operations in Vermont are now subject to 30 V.S.A. § 227d, which allows small eligible telecommunications carriers to elect a reduced form of regulation. Following the acquisition, FairPoint Vermont may not qualify for the exemption, as FairPoint Communications will serve more than ten percent of the subscriber lines in the state. Skrivan reb. pf. at 12; Campbell pf. at 42.

203. Following the acquisition, FairPoint Vermont's operation should be subject to the same pricing rules as apply to the properties that FairPoint will acquire from Verizon. Campbell pf. at 42–44.

iv. Changes to Incentive Regulation Plan

204. Verizon now markets its services across multiple states, and Vermont benefits to a degree from that, as services, packages, bundles, and prices which are offered in other states are introduced into Vermont more or less consistently across the Verizon footprint. Campbell pf. at 36.

205. One of the statutory requirements for the Board in approving, modifying, or renewing an alternative regulation plan is to establish "standards and procedures by which the effectiveness of the alternative form of regulation can be determined." 30 V.S.A. § 226b(d)). Campbell pf. at 39.

206. To implement this provision, the Board has required Verizon to file a Performance Benchmark Report as a condition of the Incentive Regulation Plan. This report provides the Board and Department with information that allows them to compare Verizon's performance on a number of measures relative to other states in which it operates. Campbell pf. at 39.

b. Discussion

The Board has traditionally examined the reasonableness of the terms and conditions of service of the new entrant in the context of acquisitions.[141] This is necessary both to ensure that they are just and reasonable (as required by Section 218(a)) and that customers are treated fairly as a result of the transaction.

i. Parties' Positions

FairPoint asserts that "the terms and conditions of service provided by FairPoint after closing will be just and reasonable, because these terms and conditions will be those under which

141. *See* Docket 6150, Order of 9/13/99 at 9–10.

Verizon provides service today."[142] In particular, FairPoint relies upon the fact that it proposes to assume Verizon's rights and obligations under the terms of the Incentive Regulation Plan, including Verizon's obligations under the SQ Plan and the Performance Assurance Plan ("PAP").[143] As part of these commitments, FairPoint will adopt Verizon's present tariffs. FairPoint also argues that wholesale customers will receive the same services provided by Verizon today on the same terms.

FairPoint further contends that its plan to deploy new, competitively-priced services and bundles will provide additional benefits. FairPoint notes that it has made commitments that go beyond those embodied in the Incentive Regulation Plan, including an agreement that, through December 31, 2010, it will not withdraw or increase the price for any regulated intrastate telecommunications service offered by Verizon as of the date of closing without Board approval and, for one year following closing, will not raise prices for non-regulated services; these additional commitments, FairPoint argues, go further to ensure that the terms and conditions are reasonable.

The Department states that, if FairPoint complies with all requirements of the Incentive Regulation Plan, Verizon's rates could be presumed just and reasonable for FairPoint as well. However, the Department maintains that, without taking into consideration "the offsetting value which Verizon is obliged to deliver through the broadband commitment and the other benefits of the plan,"[144] it is difficult to judge the reasonableness of Verizon's current rates. In addition, the Department maintains that the rates and other terms and conditions may not be reasonable if FairPoint does not comply with all conditions of the Incentive Regulation Plan, including the service quality commitments. To partially address these concerns, the Department proposes several Conditions (28, 36, 37, 42) which would require FairPoint to adopt the Incentive Regulation Plan, file tariffs matching Verizon's, and prorate volume pricing arrangements.[145]

142. FairPoint Brief at 98.

143. The SQ Plan governs retail service quality. The PAP sets out wholesale performance metrics as well as compensation mechanisms when Verizon fails to meet the metrics.

144. DPS Brief at 19.

145. FairPoint has agreed to these conditions.

The Department also expresses concern that the present arrangements, including the financial concerns discussed in the previous section, could produce a situation in which the rates would not be just and reasonable. In particular, the Department highlights the potential conflict that the Board may face in the future between resetting rates to just and reasonable levels and the need to provide FairPoint higher cash flows to keep the company financially stable.

Moreover, the Department notes that FairPoint's analysis is focused on the short-term rate levels. The Department contends that, in the future, FairPoint's rates may not be just and reasonable due to changes in FairPoint's cost structure relative to Verizon's or because the existing rates were knowingly set high in exchange for a commitment to broadband deployment that ends in 2010. To the extent any increased earnings arise from greater efficiencies, the Department does not object; however, it states that consumers should also see some of the benefits from earnings improvement.

ii. Reasonableness of Rates and Other Terms and Conditions

FairPoint's proposal includes numerous commitments that are intended to assure that its terms and conditions of service will be just and reasonable. In essence, FairPoint will provide, at a minimum, the same services that Verizon has, at prices no greater than those offered by Verizon. FairPoint plans to adopt all of Verizon's retail and wholesale tariffs and contracts.[146] FairPoint will not discontinue or interrupt any Verizon retail service and has agreed not to withdraw or increase the price for any intrastate service through the end of 2010 without Board approval.[147] The Proposed Transaction has the potential to adversely affect certain customers that have prices based upon calling volume that may include call volumes in Verizon territories that FairPoint is not acquiring; to eliminate such potential impacts, FairPoint plans to prorate the volume requirements, so that the volume pricing terms exclude volume requirements from states outside of the acquired Vermont operations.[148] FairPoint also has committed not to raise prices

146. Skrivan reb. pf. at 6; Nixon pf. at 26–27; Lafferty pf. at 18; Lafferty reb. pf. at 31.

147. Campbell reb. pf. at 35; Nixon pf. at 27. FairPoint agreed to the limitation on price increases and withdrawal in its Reply Brief. FairPoint Reply Brief at 15.

148. Campbell reb. pf. at 35; FairPoint Reply Brief at 15 and Attachment 1 at 7.

on non-regulated services (including DSL) for one year.[149] Going forward, FairPoint plans to provide all of the services necessary to qualify as an ETC. Finally, FairPoint will continue Verizon's existing arrangements with independent incumbent local exchange carriers with no change in rates, terms or conditions of the services.[150]

We also find it reasonable to apply the Incentive Regulation Plan, which the Board adopted in 2005 and 2006,[151] to FairPoint.[152] The Incentive Regulation Plan, which governs Verizon's present operations, replaces traditional regulation with an incentive structure. Under the Incentive Regulation Plan, FairPoint will have increased pricing flexibility for new services, but will be unable to raise rates for or withdraw existing services. In addition, FairPoint will keep in place, through 2010, any services now in existence.[153] This will help ensure that ratepayers do not see higher rates or less favorable terms of service as a result of the acquisition.[154] In addition, the Incentive Regulation Plan incorporates the SQ Plan as well as Verizon's broadband expansion commitment. FairPoint's adoption of the Incentive Regulation Plan necessarily includes all of these obligations.[155] Collectively, these provisions will ensure that, in terms of pricing and other terms and conditions, customers will receive the same level of services they do now.

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149. Tr. 9/5/07 at 72–76 (Leach).

150. Tr. 9/19/07 at 214–216 (Nixon); tr. 9/5/07 at 18–19 (Leach); exhs. ITC-1 and ITC-2.

151. Nixon pf. at 25–27; Skrivan reb. pf. at 9.

152. This is the first alternative regulation plan applicable to FairPoint. Normally, adoption of an alternative regulation plan would require following the procedures set out in 30 V.S.A. § 226b, and an assessment of the specific criteria included in that section. There are also no specific requirements in that section associated with the transfer of a plan from one company to another. In this proceeding, we find that it is reasonable and appropriate to transfer the Incentive Regulation Plan to FairPoint. The criteria that we have evaluated as part of our determination that the transaction promotes the general good are consistent with Section 227b's substantive criteria. In addition, all parties have had full notice since the outset of this investigation that FairPoint was seeking authorization to operate under the same terms and conditions as had Verizon.

153. Under the Incentive Regulation Plan, existing services are those that Verizon offered as of April 24, 2000, which was the start of the first Incentive Regulation Plan. FairPoint's commitment means that services offered since that date will be treated as if they are existing services, even though they are considered "new" under the terms of the Incentive Regulation Plan.

154. Lafferty pf. at 19; Nixon pf. at 27.

155. As discussed below, however, while maintaining that it is inappropriate to adjust FairPoint's Incentive Regulation Plan obligations in any way, FairPoint has simultaneously asked that we modify several aspects of that Plan that it would prefer to change.

However, FairPoint's position that its rates, terms and conditions will be just and reasonable because they mirror Verizon's rests on the assumption that those of Verizon meet this standard. Examination of the validity of this assumption requires a brief review of the Board's Docket 6959/7142 Orders that adopted the Incentive Regulation Plan and found rates just and reasonable. In that case, the Board reviewed Verizon's existing rates and other terms of service in the context of Verizon's request for approval of the Incentive Regulation Plan. We found that Verizon's then-existing rates exceeded just and reasonable levels by $8.18 million annually and required Verizon to reduce its rates by those amounts. We required Verizon to further reduce rates by $1.26 million effective July 1, 2007, and $1.80 million effective July 1, 2007, reflecting known changes in Verizon's going-forward cost-of-service. Nonetheless, in lieu of rate reductions to customers, the Board later accepted an agreement between Verizon and the Department under which Verizon committed to extend broadband services to then-unserved areas. We found that Verizon's commitment to expand broadband service — which would increase the percentage of Verizon customers with access to DSL service from 55 percent to 80 percent by 2010 — would provide significant value to Vermont ratepayers and justified not setting rates using traditional methodologies.[156] But for this commitment, Verizon would have needed to reduce rates.

Thus, we find that FairPoint's rates, terms, and conditions are just and reasonable *only* in the context of the Incentive Regulation Plan as a whole, including FairPoint's adoption of all of Verizon's commitments. This includes the broadband expansion plan. It is for this reason that, as we discuss below, we do not consider FairPoint's planned broadband expansion to be a significant incremental benefit of the transaction; Verizon is already obligated to expand out to 80 percent of its customers by 2010; ratepayers are paying for it in the form of over $50 million in rates over the term of the Incentive Regulation Plan. The Proposed Transaction's broadband

156. Dockets 6959/7142, Order of 4/27/06 at 2.

commitment provides added benefits only to the extent that it extends beyond what Verizon must now provide, since build-out to that level has been or will be funded already.[157]

Our conclusion that in the context of the Incentive Regulation Plan, FairPoint's rates, terms, and conditions will be reasonable is limited to the short term. As the Department points out, various known changes call into question whether these rates will still be just and reasonable in 2010; it is likely that some unanticipated changes will also occur. We do not need to resolve these issues, but we will examine them at the time the Incentive Regulation Plan is reconsidered.

Consistent with the above discussion, if we were to approve the Proposed Transactions, we would adopt the following conditions:

> **FairPoint shall file tariffs, to be effective on the date of closing, that match the rates, terms and conditions in Verizon Vermont's current tariffs.**
>
> **FairPoint shall be subject the terms and conditions of the 2005–2010 Amended Incentive Regulation Plan set out in Appendix A of the Board's Order of April 27, 2006, in Dockets 6959/7142 (including the 2005–2010 Amended Service Quality Plan set out in Appendix B), except as modified by this Order.[158]**
>
> **FairPoint shall prorate all volume pricing provided for in any tariff or other agreement so that the volume thresholds are reduced by the portion of the customer's volume that is generated in states outside of the acquired Verizon operations.**

iii. Transaction Costs

FairPoint has committed not to seek recovery of transaction costs. These include costs associated with any acquisition premium or amortization thereof, due diligence, negotiation, and

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157. As we discuss below, FairPoint's broadband proposal offers two potential incremental benefits. Verizon's broadband commit requires it to make broadband available to 80 percent of its access lines by 2010. FairPoint plans to achieve this result a year earlier. Exh. HBS-1. FairPoint also states that it may improve on the 80 percent penetration rate and reach up to 88 percent of its access lines, although it neither promises this outcome nor does it know if it will be met. Tr. 9/18/07 at 44–45 (Brown). In addition, FairPoint will be using different DSL protocols, which may provide customers with improved broadband speeds.

158. The Department also requested that we adopt a condition requiring FairPoint Vermont to adopt the Incentive Regulation Plan for its Vermont operations. We discuss that condition below.

costs to obtain financing.[159] However, FairPoint plans to capitalize some costs. These include costs arising from the Capgemini contract associated with acquiring, developing and implementing systems which will serve in the place of existing Verizon systems and for which costs are currently allocated to its Vermont operations by Verizon.[160] FairPoint states that it may seek rate recovery of these costs.[161]

The Department generally agrees with FairPoint's proposal. However, the Department also asserts that increased costs due to FairPoint's need to develop and transition to new systems currently supported by Verizon, or which are incurred as a result of reliance on Verizon under the Transition Services Agreement ("TSA"), should also not be recoverable from ratepayers in any future ratemaking proceeding.[162] It proposes Condition 8 to address this concern.

We agree with the Department and FairPoint that transaction-related costs should not be recoverable in future rates. Such recovery would essentially require ratepayers to pay for the privilege of being acquired, by including in rates costs that are only necessary because of the transaction. The Department and FairPoint do not fully agree on what constitutes transaction-related costs, however. In general, as the Department suggests, increased costs associated with the development of new systems should not be recoverable, for the same reason as transaction costs. At this time, however, we do not need to resolve exactly which costs will be excluded, nor can we, given the absence of specific information on the category of costs. We will address this matter during the next proceeding that examines FairPoint's rates.

If we were to approve the Proposed Transaction, our Order would reflect the ruling on transaction costs by adopting the following condition:

> **FairPoint may not recover in rates any expenses related to the transaction or the transition from Verizon to FairPoint, including any acquisition premium or any increased costs which are due to FairPoint's need to develop and transition to new systems currently**

159. Skrivan reb. pf. at 20; Leach pf. at 35; tr. 9/20/07 at 116–118 (Nixon); Nixon pf. at 27.

160. Skrivan reb. pf. at 21; exh. FP Cross 3.

161. Skrivan reb. pf. at 20; tr. 9/7/07 at 186–192; 207–213 (Skrivan); exh. FP Cross 3. By contrast, FairPoint plans to treat costs incurred under the TSA as operating expense. Skrivan reb. pf. at 21. Due to the Incentive Regulation Plan, there would be no mechanism for recovering such costs.

162. Campbell pf. at 16 and 47.

supported by Verizon, or which are incurred as a result of continued reliance on Verizon under the Transition Services Agreement.

iv. Modifications to the Incentive Regulation Plan

Although it states that it will adopt the Incentive Regulation Plan, FairPoint seeks to modify two provisions. First, FairPoint proposes to modify the Performance Benchmark Report so that it would cover only the three northern New England states rather than all of the Verizon states in the former Bell Atlantic footprint. Second, FairPoint, also objects to any requirement that it continue to offer existing Verizon bundles of services.

The Department seeks several other modifications to the Incentive Regulation Plan. Concerning the Performance Benchmark Report, the Department proposes Condition 47 which would require FairPoint to obtain a legally binding commitment from Verizon to continue to provide the information in the report. The Department also requests that we adopt Condition 38, to limit the definition of new services in the Incentive Regulation Plan to encompass only those services that FairPoint introduces after the acquisition, so that any service that Verizon offers as of the date of closing would be considered an existing service.[163] This would require that FairPoint "implement bundles or packages with the same terms, conditions and pricing as Verizon" that would apply at least "until FairPoint files the appropriate tariffs and obtains specific approval to change the bundles or packages in any way."[164] The Department asks (proposed Condition 39) that we modify the Incentive Regulation Plan to require that FairPoint treat any changes in Universal Service Fund ("USF") support as exogenous changes. Finally, in conditions 49 and 50, the Department asks that we adopt conditions that would change the scope of the broadband commitment in the Incentive Regulation Plan.

As to the Performance Benchmark Report, FairPoint and Verizon assert that much of the information now provided in those reports will no longer be relevant as Verizon's performance in those jurisdictions will no longer be an appropriate basis for comparing FairPoint's performance in Vermont. In addition, Verizon maintains that some of the information is confidential, so that Verizon could not disclose it without potentially waiving confidentiality. The Department argues

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163. *See* fn. 153.

164. Skrivan reb. pf. at 22; *see* Lafferty pf. at 35.

that a comparison to other Verizon states is still meaningful in assessing whether Vermont consumers are receiving adequate value under the Incentive Regulation Plan. In addition, the Department asserts that it would be more difficult to assess the effectiveness of the Incentive Regulation Plan without such information.

The primary purpose of the Performance Benchmark Report was to provide data to compare whether Vermont consumers were receiving fair value relative to other Verizon states, by examining both the price and range of service offerings. These comparisons were adopted because, under incentive regulation, there is less connection between prices and costs. To evaluate the fairness of prices, we considered how they compared to those in other states as well as how the services compared. We did not limit the comparison to northern New England or even New England as a whole; we expected that the incentives in the Incentive Regulation Plan would enable Vermont consumers to receive value comparable to that of other Verizon ratepayers. We continue to believe that this is a fair point of comparison. Adoption of FairPoint's proposal would change the reference point to encompass only the three northern New England states. It would also mean that Vermont consumers should recalibrate their reasonable expectations of value. We see no reason that the sale should cause us to make such a change.

We recognize that it may be difficult for FairPoint to obtain all of the information required by the report. We also understand Verizon's reluctance to agree now to provide the information. Nonetheless, for the reasons outlined above, we will require FairPoint to continue to provide the Performance Benchmark Report as now constituted. We do not adopt the specific requirement recommended by the Department (*i.e.*, a legally-binding commitment from Verizon). Instead, if we approved the Proposed Transaction, we would adopt the following condition requiring FairPoint to provide, prior to closing, an assurance that it will provide the same information and an explanation of the arrangements that it has made that guarantee access to the information.

> **FairPoint shall assume Verizon's duty to provide annually a Performance Benchmark Report. FairPoint shall demonstrate that it has made arrangements to include all state-specific information currently described in that report.**

The Department's proposed change to the treatment of new services appears to be largely addressed through a condition to which FairPoint and the Department have agreed. Specifically, these parties now propose that FairPoint will maintain all services in effect at the time of closing through 2010, absent Board approval to modify or withdraw the service. This has the same effect as resetting the definition of "new services" to the date of closing. It also means that FairPoint must keep in effect all bundles that Verizon now offers, absent specific permission to change or discontinue them. If we approved the Proposed Transaction, the condition we would adopt reads as follows:

> **Through December 31, 2010, FairPoint shall not withdraw or increase the price on any regulated intrastate telecommunications service offered by Verizon under tariff as of the closing date of this transaction without the approval of the Board.**

Turning to the treatment of changes in federal USF support, we find that the current Incentive Regulation Plan ensures that cost and revenue changes can flow through to ratepayers. First, the Incentive Regulation Plan now allows for an adjustment to rates to reflect changes in USF support to the extent that they exceed $1,000,000. Section II.A.2.a.iv provides specifies that the following may be considered exogenous costs:

> Regulatory, judicial, or legislative changes affecting the telecommunications industry, including rules and orders that are necessary to implement such changes.[165]

This provision was designed to encompass changes in USF. In fact, in Dockets 6167/6189, the Board considered a Department proposal that would have excluded USF changes from treatment as exogenous costs, deferring them instead to other investigations. The Board rejected this proposal, observing that:

> The Department's proposal also would not require Bell Atlantic to flow through any changes in Universal Service funding under Section 254 of the Act; these changes should be automatic, since they are outside the Company's control.[166]

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165. Dockets 6959/7142, Order of 4/27/06, Appendix A at 2.

166. Dockets 6167/6189, Order of 3/24/00 at 18–121. The exogenous cost provisions of the Incentive Regulation Plan are identical to those in the 2000 Incentive Regulation Plan.

This language makes clear our intent that exogenous cost and revenue treatment would encompass any change to USF funding, whether the result of federal changes to the USF or regulatory approval of ownership changes that would have the affect of altering USF funding.[167]

The second reason we question the need for the Department's proposal is that it fails to take into account the manner in which USF has been treated. A portion of the USF funds are included as part of Verizon's overall revenues. However, for a number of years, the bulk of USF funding has not been flowed through the normal cost-of-service and rates, but has instead been passed on to ratepayers in the form of a direct, negative surcharge.[168] It has been adjusted as necessary to reflect changes in USF funding, not as exogenous costs, but directly. We would expect FairPoint to continue this practice, which results in a direct pass-through of annual changes to USF support.

Notwithstanding our conclusion that a modification to the Incentive Regulation Plan is appropriate, if we approved the Proposed Transaction, we would adopt the following condition, consistent with the Department's recommendation, to eliminate any ambiguity about the need to pass through any increased USF funding.

> **Notwithstanding any other provision of the Incentive Regulation Plan, the Board or the Department may seek rate reductions commensurate with any increase in Federal Universal Service Funding which the Vermont operation may be eligible to receive as a direct or indirect result of the transaction.**

The Department's final set of proposed conditions relate to the broadband deployment plan to which Verizon is not subject. The Department asks first that we state that lines will be considered broadband-qualified for proposed of the Incentive Regulation Plan only if the upload and download speeds are equivalent to those in New York, Rhode Island, and Massachusetts at prices no higher than in those states. The Department asserts that such benchmarking of service offerings is consistent with the goal of the Incentive Regulation Plan that Verizon provide

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167. We would be surprised to see a company such as FairPoint argue that any change to USF funding, which is designed specifically to support consumers, should not be flowed through.

168. *See* Verizon Tariff No. 20, Part M, Section 1.1.4; tr. 9/17/07 at 158–161 (Porell). Pursuant to 3 V.S.A. § 810, we hereby take administrative notice of Verizon's Tariff No. 20. Any party that objects to such notice shall submit its objection within 10 days of this Order.

equivalent value in Vermont relative to other states. FairPoint opposes this recommendation. FairPoint states that the proper point of reference should be Vermont, not broadband deployment in other states which may be based upon FTTH. FairPoint does agree to match data speeds and prices with the services that are in existence in Vermont at the time of closing.[169]

For several reasons, we decline to adopt the Department's recommended condition. As written, it is not clear how the comparison would be made to other states. As FairPoint suggests, the Department has shown no basis for requiring it to meet a FTTH standard. Even if we interpreted the Department's recommendation to exclude FTTH installations, it would still be difficult to conduct a meaningful comparison. In addition, FairPoint's broadband deployment plans coupled with our adoption of the Department's consistent coverage plan should go a long way towards addressing the Department's concerns. FairPoint will be deploying a new protocol that should provide consumers with increased speeds relative to Verizon's DSL offerings. The condition we adopt for the consistent coverage plan requires a minimum speed of 1.5 Mb/s.

Although we decline to adopt the Department's recommended condition, we continue to view the remaining states in the old Bell Atlantic footprint as a meaningful point of comparison for services and prices. The comparison the Department seeks to make absolute will still be a valid consideration during our next consideration of the Incentive Regulation Plan and the value that FairPoint has provided under the flexibility that we allow.

The Department's final recommended condition is to exclude certain lines served out of the Burlington Central Office from the calculations of additional broadband lines for purposes of complying with the Incentive Regulation Plan. The Department states that this was the intent of the agreement between it and Verizon in Dockets 6959/7142, which led to the Incentive Regulation Plan. FairPoint agrees to this condition. If we approved the Proposed Transaction, we would adopt the following:

> **Additional lines or line equivalents qualified for broadband service in the territory served out of the Burlington Central Office after July 1, 2005, shall be excluded from the number of additional lines qualified for broadband service for purposes of the calculations under the Incentive Regulation Plan.**

169. Harrington/Brown/Smee reb. pf. at 32, 37.

v. Regulation of FairPoint Vermont

At the present time, a FairPoint subsidiary operates in Vermont. This subsidiary, FairPoint Vermont, has elected to be regulated under 30 V.S.A. § 227d, which allows "a carrier which serves fewer than ten percent of subscriber lines installed in the aggregate statewide and has been designated as an eligible telecommunications carrier in a service area where a competitive eligible telecommunications carrier has also been designated" to elect to be exempt from one or more specified statutory requirements that would otherwise apply to it; the exemption largely encompasses rate regulation. The Department asserts that, with the approval of FairPoint's acquisition of the Verizon properties, FairPoint Vermont will no longer be eligible for such treatment as the combined holdings of FairPoint will far exceed the 10,000 access line threshold. However, rather than causing FairPoint Vermont to return to traditional rate-of-return regulation, the Department recommends that the Board require that FairPoint Vermont be covered by the terms of the Incentive Regulation Plan and proposes three Conditions (43, 44, and 48) to effectuate these proposals.

FairPoint disagrees with the Department on FairPoint Vermont's continued eligibility for regulation under Section 227d. FairPoint has committed that, in the future, it will combine its existing Vermont operations with the newly-acquired company. However, for the present, FairPoint argues that FairPoint Vermont should retain the exemption under Section 227d and not be covered by the Incentive Regulation Plan.

Section 227d does not explicitly address the situation in which two companies with common ownership exceed the 10 percent threshold whereas one (or both) of them separately do not. As the Department asserts, the combined FairPoint operations will far exceed the statutory threshold for eligibility. Nonetheless, the statute uses the term "carrier," but it does not specify whether in determining whether a company is a carrier one should look narrowly at the operating company (thereby accepting the corporate structure) or more broadly at the overall corporate ownership. The language seems to imply the former, in which case FairPoint Vermont would retain its exemption. The intent of the legislature, however, is clearly to limit the exemption to small telecommunications carriers. We conclude that, in light of this intent, we should interpret the term "carrier" to encompass the ultimate ownership. To do otherwise creates incentives for companies to break up solely to avoid regulation. Following the merger, FairPoint and its subsidiary, FairPoint Vermont, will jointly operate the vast majority of the access lines in the state. In light of this fact, allowing FairPoint Vermont to retain its exemption makes little sense; carriers owned by the same broader corporation should be treated similarly in terms of regulation.

We also agree with the Department that, rather than forcing FairPoint Vermont to return to traditional regulation, it is reasonable to continue to allow it to have some flexibility on deployment of new services.[170] The Incentive Regulation Plan provides a framework under which FairPoint Vermont would continue to have such flexibility. The Incentive Regulation Plan has four primary components: pricing, service quality, annual investment, and broadband deployment. For existing services, rates are frozen and the service must remain in place absent Board approval.[171] For new services, including combinations of existing service in a new package, Verizon (and therefore, FairPoint) is free to price the service as it chooses. Requirements for prior Board review are also reduced. The Incentive Regulation Plan also incorporates the SQ Plan to address retail service quality and requires that Verizon comply with wholesale service quality standards that the Board adopts. On investment, the Incentive Regulation Plan does not specify minimum investments, but instead mandates that Verizon maintain at all times a level of investment and operating expenditures sufficient to maintain the integrity of the network, reliability, and availability of service. Finally, the Incentive Regulation Plan incorporates a broadband deployment plan, which we discuss in detail below in Section V.E.[172]

To provide FairPoint Vermont continued pricing flexilibity for new services, we adopt the Department's proposed condition to apply the pricing terms of the Incentive Regulation Plan to FairPoint Vermont. We would also adopt the provisions in the Incentive Regulation Plan that

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170. The Department explicitly raised FairPoint Vermont's regulation and the section 227d exemption as an issue in this case. To the extent that the exemption is not automatically terminated, we interpret the Department's request as one under subsection 227d(c) to revoke the exemption.

171. The Incentive Regulation Plan includes exceptions that would allow Verizon to adjust existing rates in the event of certain changes in costs or revenues that are outside the company's control.

172. Docket 6959/7142, Order of 4/27/06, Appendix A.

apply to investment. FairPoint Vermont would not be subject to the SQ Plan[173] or the broadband commitments in Appendix A to the Incentive Regulation Plan. For this reason, FairPoint's progress towards meeting the broadband commitment in the Incentive Regulation Plan and its additional broadband plan offered in this proceeding, shall be measured using only access lines in the previous Verizon service territories. If we approved the Proposed Transaction, we would adopt the following conditions:

> **The election of FairPoint Vermont under 30 V.S.A. Section 227d is terminated; FairPoint Vermont shall be included in the provisions of the Incentive Regulation Plan related to changes in pricing, terms, and conditions of service.**
>
> **The FairPoint Vermont lines shall be excluded from measurements of progress toward the Incentive Regulation Plan's broadband deployment milestones.**
>
> **FairPoint Vermont shall comply with the Annual Investment requirement of the Incentive Regulation Plan**.

2. Adequate service quality (retail)

a. Findings

i. Verizon's Service Quality

207. The SQ Plan is incorporated into Verizon's Incentive Regulation Plan and establishes the process under which the Board monitors Verizon's service quality commitments. The SQ Plan tracks many standard industry performance metrics and includes a service quality compensation payment mechanism under which customers receive compensation for Verizon's failure to meet the baseline standard for any of the performance areas in the plan. Lafferty pf. at 21.

208. Verizon has not met all of the standards resulting in service quality compensation payments to customers for non-compliance each year since the inception of the first SQ Plan in 2000. More recently, Verizon has met the baseline for all of the service quality metrics in the SQ

173. However, as the Department recommends, for each measure in which a Docket 5903 and SQ Plan standard evaluate the same performance, FairPoint Vermont should submit its service quality reports using the standards and benchmarks in the SQ Plan, rather than the Docket 5903 standards.

Plan except for the metric measuring % Residence Troubles Not Cleared in 24 Hours. Pariseau pf. at 2; Pariseau sur. pf. at 3–4; Lafferty pf. at 21; Wierson pf. at 4–5; Porell reb. pf. at 4–5.

209. Since 2002, Verizon has consistently failed to achieve the standard for residential trouble report clearing and its monthly performance has consistently been below the baseline standard. Pariseau pf. at 2; Lafferty pf. at 21; Harrington/Brown/Smee reb. pf. at 13; tr. 9/18/07 at 38–39 (Smee); tr. 9/21/07 at 14 (Nixon); tr. 9/17/07 at 149 (Porell).

210. In 2000 and 2001, Verizon easily met the standard for Residential Trouble Not Cleared in 24 Hours, reporting annual rolling averages of 20% and 24.3%, respectively, compared to a baseline of 30%.[174] Pariseau sur. pf. at 5; Peres reb. pf. at 20.

211. Verizon's performance in a number of other measurements has shown a decline rather than an improvement even where Verizon has continued to meet the standard. From 2001 to 2006, Verizon experienced an 87% increase in the percentage of residential out-of-service conditions not cleared within 24 hours, a 54% increase in the percentage of business out-of-service conditions not cleared within 24 hours, a 26% increase in the percentage of calls not answered by the company within 20 seconds, and a 75% increase in the percentage of missed installation appointments. Pariseau sur. pf. at 13; Peres pf. at 13; Peres reb. pf. at 18–19.

212. Verizon has had to pay a significant amount due to non-compliance since the inception of the first SQ Plan, particularly since 2003. In that year alone, Verizon had to pay $8 million. The compensation payments appear to have been too small to have much of an impact on Verizon. Lafferty pf. at 21; Docket 5957, Order of 6/1/05 generally.

213. Often a consumer has had to notify Verizon and the Department numerous times before the problem is identified and remedied. In the meantime, many of the prior trouble tickets have been cleared by Verizon as "suspected CPE" referring to the Customer Provided (or Premises) Equipment, leaving the consumer frustrated and without resolution to their complaint of poor telephone service. Pariseau sur. pf. at 7.

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174. The standard of 30% means that Verizon is required to clear 70 percent of residential troubles within 24 hours of being reported. From the customer's perspective, this means that Verizon will meet its standard even if 30 percent of customer troubles remain unresolved within a day.

ii. FairPoint Vermont's Historic Service Quality

214. From 2002 through 2006, FairPoint Vermont has not missed a baseline or action level benchmark. However, because of its size, FairPoint Vermont does not report on Performance Measurement #3, Calls Not Answered within 20 seconds, Residence. Pariseau pf. at 4; Campbell pf. at 21.

215. FairPoint Vermont has shown a consistent ability to clear residential-customer troubles within 24 hours for its existing Vermont operations under the 35% (baseline)/ 45% (action level) standard made applicable to it in Docket No. 5903. From the start of 2005 through the first half of 2007, FairPoint Vermont has cleared over 95% of residential troubles within 24 hours, based on a rolling annual average. Exh. FP-Cross 13.

216. FairPoint Vermont's reported service quality metric does not compare favorably to other Vermont companies similarly situated to FairPoint Vermont and regulated under the same standard. Pariseau pf. at 5–6.

217. FairPoint has had service problems in Maine where it is the second largest ILEC. Lafferty pf. at 26 and 28.

iii. Service Quality of FairPoint After Acquisition

218. FairPoint proposes to assume Verizon's obligations under the SQ Plan and will comply with service quality standards, consumer protection standards, and requirements set forth in relevant Board Orders. Nixon pf. at 25; tr. 9/6/07 at 149–50 (Leach).

219. The service quality compensation penalties under the SQ Plan should serve as an incentive for FairPoint to meet the SQ Plan's service quality standards and should represent a greater incentive for FairPoint to comply with the standards than such penalties have had for Verizon. Tr. 9/21/07 at 14–15 (Nixon); tr. 9/21/07 at 10 (Wheaton); Lafferty pf. at 19–20.

220. The potential for losing customers and revenues due to competition is likely to have a more material impact on FairPoint's ability beginning to provide alternatives to certain customer groups which can impact FairPoint's top line in the form of reduced customer lines, services and revenues. Unlike for Verizon, the acquired Vermont operation will be one of the largest properties for FairPoint overall; lost customers and revenues in Vermont will adversely affect

FairPoint's ability to continue growing and paying the dividends its investors expect to receive. Lafferty pf. at 20.

221. In addition to the SQ Plan, FairPoint plans to establish key performance indicators ("KPIs") by functional area of responsibility, and there will be service quality objectives identified within each organization. Nixon reb. pf. at 20, 23; tr. 9/20/07 at 150.

222. The Verizon work force will continue with FairPoint at closing, and FairPoint plans to add additional personnel, which will allow it to begin an enhanced proactive maintenance program. Tr. 9/17/07 at 218–219 (Smee).

223. FairPoint intends to meet the % Residence Troubles Not Cleared in 24 Hours metric of 30% and has proposed solutions to address the problem. These include adjusting the manner in which repair calls are dispatched and ensuring that it has adequate technician staff to handle the volume of trouble reports. FairPoint plans to add at least six installation and maintenance ("I&M") technicians to the force specifically to address the 24-hour clearance metric for residential customers. Harrington/Brown/Smee reb. pf. at 13; tr. 9/17/07 at 207, 218–19 (Smee); tr. 9/18/07 at 40-41 (Smee); Nixon reb. pf. at 28, 31.

224. FairPoint has identified some outside plant where maintenance is behind schedule; FairPoint also proposes to increase proactive, preventative maintenance and has budgeted amounts to address these maintenance issues. Tr. 9/18/07 at 38–39 (Brown, Smee).

225. As FairPoint continues to gain a higher level of detail from Verizon, including the knowledge it will gain from the work force after close, it will identify and build a plan for any localities where a focused rehabilitation of the plant will both reduce the volumes of troubles and thus relieve stress on the I&M forces in their efforts to restore service quickly on the fewer troubles which are reported. Harrington/Brown/Smee reb. pf. at 14; tr. 9/17/07 at 212–213 (Smee); tr. 9/18/07 at 41–44 (Smee).

226. FairPoint will analyze the network trouble report rates to identify those portions of the network that require rehabilitation; FairPoint will then put together a plan to rehabilitate those areas. Tr. 9/17/07 at 211–212 (Smee).

227. While clearing troubles in a timely fashion is a measure of service quality, having a lower number of troubles overall allows for better service. The network trouble report rate is the

leading indicator of the quality of the infrastructure; if customers are not reporting troubles, the network is likely to be providing quality service. Tr. 9/17/07 at 216 (Smee); Harrington/Brown/Smee reb. pf. at 14.

228. Verizon's statewide network trouble report rate has been less than 1.4, within the baseline standard required by the SQ Plan. Tr. 9/17/07 at 216 (Smee); Harrington/Brown/Smee reb. pf. at 12; *see* Pariseau sur. pf. at 3.

229. The low statewide average does not mean, however, that particular wire centers are not experiencing troubles, and that such wire centers would benefit from greater attention. Tr. 9/17/07 at 206 (Smee).

230. Trouble report rates can be very volatile when viewed by individual wire center; a single event in a small town can have a large effect on the trouble report rate for any given month. Tr. 9/17/07 at 208 (Smee).

231. Service quality issues which may be localized are not tracked and reported as part of the service quality performance standards. These problems are not easily identified and have often continued for years, with the affected consumers suffering from frequent interruptions of service which may last hours or days. Pariseau sur. pf. at 6–7.

232. Verizon has recently taken steps to address some of these localized issues. Porell reb. pf. at 7–8.

233. To identify trouble spots FairPoint plans to use the network trouble report rates as well as other information on outside plant condition. Tr. 9/17/07 at 203–204 (Harrington, Smee).

234. Verizon's customers have also experienced delays in line extensions due to a lack of facilities, sometimes resulting in consumers waiting months for the installation. In some instances, consumers have been required to pay for the installation of new service, with poles and lines, only to have the installation delayed up to 6 months or longer. Pariseau pf. at 8.

235. The preventative maintenance work in the field will also occur during the winter months when order rates are down and trouble report rates are typically lower. Tr. 9/18/07 at 42–43 (Smee).

236. FairPoint has committed that, if the trouble report rate for any given wire center exceeds twice the statewide standard of 1.4 for three consecutive months, it will develop a remediation

plan to address the issues causing the higher trouble rate and present that plan to the Department for its review. Tr. 9/17/07 at 208, 210–11 (Smee).

iv. Quality Assurance Plan

237. The transition of Verizon wireline assets in Vermont along with New Hampshire and Maine is a complex and detailed operation. Tasks of extracting data have been outlined in the Verizon cutover plan . All databases and other information delivered to FairPoint must be integrated into their systems and checked or audited prior to the full operational cutover. Many opportunities exist for failure, including the following:

- Missing files or records from incomplete transfer
- Verification of Verizon databases prior to transfer
- Software incompatibility and database configuration mismatch
- Data extracts done in multiple stages containing conflicting data
- Data verification incomplete
- Testing databases in FairPoint systems
- Operational cutover with mismatched data between Verizon and FairPoint
- Field operations policies and procedures cutover from Verizon to FairPoint
- Establishment of new processes for daily operations in central offices and outside plant.

Wierson pf. at 19.

238. There are risks associated with the integration of the OSS with the network elements. FairPoint will not receive any of the Element Managers used by Verizon to manage the equipment in their network. The Element Manager provides the interface between the Network Management System in the OSS and the equipment in the network. Moreover, no provisioning or monitoring can take place unless specialized applications are developed for each equipment type in the Network Management System. This can be costly, and configuration control (especially software) could become unmanageable as network elements are upgraded. Wierson pf. at 20.

239. FairPoint has not produced for review a Management Plan or Quality Control Plan that addresses Quality Assurance (QA) and Quality Control (QC). Wierson sur. pf. at 8.

240. The reporting structure is not clear on how focus will be directed to resolve many of the existing service issues today and how FairPoint will minimize service problems in the future. System metrics are not defined. The quality team is not defined, nor how they will establish over-site or control over the quality of the network. Wierson sur. pf. at 8.

b. Discussion

i. Parties' Positions

FairPoint asserts that it is committed to providing high service quality in those areas where Verizon has been successful and to improving service quality in those areas where Verizon has been challenged. FairPoint contends that it presently provides a high level of service quality in its existing territories. FairPoint maintains that the existing Verizon network is in generally good condition and is providing good basic service; FairPoint states that it has both the intent and the capability to improve on Verizon's performance by addressing the areas in which Verizon is not meeting service quality standards as well as localized problems that have not resulted in violations of service quality standards.

FairPoint has committed to several specific measures to address service quality concerns. FairPoint stated that it will track network trouble rates, and troubles not cleared in 24 hours, by wire center as requested by the Department. FairPoint has also agreed to monitor individual exchanges and will submit a report within six months of closing that identifies specific exchanges that have exceeded a trouble rate of 1.4 for three consecutive months. To augment that commitment, FairPoint proposes that, if trouble report rates for any given wire center exceed twice the statewide standard for three consecutive months, it will develop a remediation plan to address the issues causing the high trouble rate. That plan would be submitted to the Department for its review.

Verizon echoes FairPoint's assertions, arguing that the evidence demonstrates that it now provides high quality service to its customers and that its network is well-maintained. Verizon notes that the Board examined Verizon's service quality during the 2005 and 2006 review of the SQ Plan and decided not to adjust it. Verizon contends that the same result is warranted here.

Verizon also maintains that its plant is in good condition, relying upon FairPoint's assessment of the network and the low trouble report rate.

The Department disagrees with the Petitioners, arguing that Verizon's performance "has been dismal, and the resulting penalties evidently have done little to deter Verizon from continuing to shortchange its customers, never mind improve the quality of its service." The Department expresses several concerns about FairPoint's ability to provide high quality service, given its experience and Verizon's performance. The Department asserts that FairPoint is untested as an operator of large telecommunications properties; according to the Department, FairPoint's existing service quality in Vermont (measured by its performance as an operator of FairPoint Vermont) has been worse than that of other independent telephone companies. In addition, the Department contends that FairPoint has not specifically identified the corrective actions necessary to improve service quality. The Department also questions FairPoint's ability to improve service quality and maintain it at acceptable levels considering FairPoint's financial projections that assume a reduction in operating costs and personnel over time. Moreover, the Department argues that FairPoint will have a difficult task managing a transition, that will further challenge its ability to meet service quality standards.

Because of these concerns, the Department argues that FairPoint must be provided significant incentives to meet the requirements of the SQ Plan. In particular, the Department asks that the Board:

- specifically require that the SQ Plan apply in Vermont (Condition 28);[175]
- require FairPoint to freeze dividend or other payments from its acquired Vermont property to FairPoint if the service quality standards in the SQ Plan are not being met (Condition 6);
- require FairPoint to provide the Department with the codes to be used in the new trouble tracking system to ensure the codes will provide the same information as reported by Verizon, and ensure that the codes map to Verizon's system used as a basis for the report (Condition 21);

175. The SQ Plan is a part of the Incentive Regulation Plan. We discuss FairPoint's commitment to the Incentive Regulation Plan as a whole in the preceeding section and adopt a condition requiring FairPoint to comply with the Incentive Regulation Plan.

- require FairPoint to perform on all of Verizon's obligations under the settlement in Docket 6957 (Condition 51); and
- require FairPoint to complete the projects identified by Verizon to address localized service quality issues (Condition 12).

The Department also contends that the SQ Plan, because it tracks measures on a state-wide basis, does not adequately address localized problems. Accordingly, the Department asks that we require FairPoint to use their new system, currently under development, to track on a monthly basis, Trouble Report Rates and Troubles Not Cleared in 24 Hours by exchange and ensure that no exchange has a rate on any of these measures that exceeds twice the statewide standard (Condition 1). The Department requests that FairPoint be required to provide this report to the Department upon request, but would not have to provide a monthly submission of the report to the Department.

Labor asserts that there is a substantial risk that FairPoint's service quality and customer service will not be adequate. Labor notes that Verizon's existing service quality is below acceptable levels, which will require FairPoint to expend resources simply to correct these problems — a task that will be difficult to achieve considering what it considers to be FairPoint's poor financial situation. In addition, Labor contends that this task will be made more difficult through the likely loss of many experienced Verizon workers that would otherwise be transferred to FairPoint as part of the transaction.

Labor argues that, if the Board approves the transaction (which it recommends against), we should adopt several conditions to help protect customers. First, Labor argues that we should require FairPoint to be subject to the SQ Plan, extend the term of that SQ Plan to five years from cutover, and amend the SQ Plan to impose double penalties for each category in which substandard service is delivered for two years in a row, and double the total dollar amount at risk. Labor also recommends that we tighten two standards (repair and call answer times) and add a measure for individual exchanges that have more significant variances from the baseline. Finally, if FairPoint fails to meet any individual benchmark for three consecutive years, Labor recommends that we require FairPoint to conduct an extensive service quality audit that would document the reasons for poor service quality performance and make specific recommendations to improve service quality.[176]

ii. Service Quality Expectations under FairPoint

Since 2000, Verizon has operated under a service quality plan — jointly proposed by Verizon and the Department — that the Board adopted as part of the first Incentive Regulation Plan.[177] The SQ Plan contains several standards; failure to attain the SQ Plan's standards results in penalty points, with each penalty point resulting in the payment of penalties. The penalty amounts are constructed so that penalties are not linear. Instead, over certain thresholds, additional penalty points lead to an increase in the dollar amount of the penalty per penalty point. This was developed to create financial incentives to encourage Verizon to meet the standards.[178]

Two years ago, we examined Verizon's service quality performance as part of Verizon's request to renew the Incentive Regulation Plan. At that time, we stated:

> Verizon argues, among other things, that its performance under the 2000 Service Quality Plan has been "good" and therefore an indication that a successor service quality plan is not necessary. Verizon's performance as measured by the 2000 Service Quality Plan does not support that conclusion. Rather, Verizon's performance has shown a pattern of deteriorating service quality.[179]

This conclusion remains true today. Although Verizon has met the majority of the service quality standards since the inception of the SQ Plan, in every year, Verizon has paid some penalty. In 2003, Verizon failed to attain three of the service quality standards, leading to penalties of $8 million.[180] One standard in particular has proved troublesome to Verizon: residential repairs. Under this standard, Verizon is required to repair 70 percent of customer out-of-service problems within 24 hours. Although Verizon initially met this standard, it has

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176. Labor Brief at 43.

177. The SQ Plan was renewed as part of the Incentive Regulation Plan we adopted in 2005 and 2006. Docket 6959, Order of 9/26/05 at 123–135 and Dockets 6959/7142, Order of 4/27/06, Appendix B.

178. *See* generally, Dockets 6167/6189, Order of 3/24/00 at 144–146; Docket 6959, Order of 9/26/05 at 133–134.

179. Docket 6959, Order of 9/26/05 at 128.

180. Docket 6957, Order of 6/1/05 at 2.

consistently failed to do so since 2002.[181] It appears that this failure is largely a function of inadequate resources;[182] FairPoint believes that it can, through the addition of personnel, meet the standard. If so, it would suggest that Verizon's inability to meet the residential repair standard was a choice it made.

Evaluating Verizon's performance solely on the basis of the standards in the SQ Plan also misses certain elements of Verizon's service quality. On many measures, Verizon's performance has slipped even though it continued to meet the specific standard. In addition, the SQ Plan is an aggregate measure, calculated on a statewide basis. As a result, it can mask some localized service quality shortfalls. For example, several individual exchanges have seen chronic service quality problems;[183] these instances, affecting a limited part of the state, do not lead to violations of the SQ Plan standards, even though customers are obviously affected.

In order to meet its service quality obligations under the SQ Plan, as well as its broader duty to provide adequate service quality, FairPoint will, at a minimum, need to improve on Verizon's performance in some areas while maintaining its level of service in areas in which Verizon has been successful. As we discuss above concerning FairPoint's financial model, we have significant concerns that FairPoint may face financial difficulties. If that were to occur, FairPoint may face pressure to reduce operating costs, including personnel, in an effort to maintain adequate cash flows to the parent corporation. This, in turn, could lead to diminished service quality. To address this concern, we are requiring FairPoint to provide additional demonstrations related to its financial status designed in part to make sure that FairPoint's Vermont operations will have adequate funds to meet service quality obligations irrespective of the broader company profitability.

Assuming that FairPoint can provide these financial assurances, we expect that FairPoint will be able to meet its service quality obligations (subject to the conditions we set out below). FairPoint has agreed to be subject to the SQ Plan. This Plan was designed to ensure that, as competitive pressures hit the telecommunications industry, Vermont consumers did not

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181. Pariseau pf. at 2.
182. Pariseau pf. at 3–4.
183. Pariseau pf. at 4.

experience reduced service quality as a result. For Verizon, the SQ Plan does not appear to have been an adequate deterrent for poor service quality. There are no indications Verizon has a solid plan to correct these costly service problems if it remains the service provider in Vermont.[184] By contrast, FairPoint is a much smaller company. We anticipate that the penalty amounts set out in the SQ Plan will provide a greater incentive for FairPoint to meet the standards than they have for Verizon.

In addition, FairPoint has stated that it intends to increase its workforce, including the outside plant workers. Staffing issues appear to have contributed to Verizon's inability to meet service quality and delivery deadlines.[185] As Labor points out, the most direct way to improve service quality is to allocate more capital and labor resources directly to service quality.[186] More outside plant workers will help reduce the delays customers face in getting new services installed and troubles repaired.

FairPoint also has worked to develop a plan to improve performance on the residential repair standard, which Verizon has consistently failed to achieve.[187] The increased personnel are a part of this effort, but FairPoint has identified other changes that should help it correct residential troubles more quickly.[188] FairPoint's plans also include addressing the localized problems that have led to poorer service quality in certain locations.

We are also not persuaded by Labor's concern that the Proposed Transactions will result in a significant departure of experienced personnel, leading to deteriorating service quality. Labor's assertions are based largely on a single survey it performed in the context of its opposition to FairPoint's acquisition. Labor presented no objective analysis suggesting that a large exodus of personnel was likely. While the loss of many trained outside-plant workers could adversely affect service quality, the evidence is not sufficient to show that such an event is likely.

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184. Lafferty pf. at 21; Pariseau sur. pf. at 8.

185. Wierson pf. at 14; Pariseau pf. at 3.

186. Peres pf. at 15.

187. Harrington/Brown/Smee reb. pf. at 13; tr. 9/17/07 at 207, 218–19 (Smee); tr. 9/18/07 at 40-41 (Smee); Nixon reb. pf. at 28, 31.

188. *See* finding 223.

iii. Conditions

The parties have proposed several conditions intended to improve the service quality. FairPoint has agreed to the Department's proposal to require it to track Troubles Not Cleared in 24 hours at the wire center level (starting at cutover) and ensure that no exchange has a trouble report rate greater than twice the statewide standard. If the trouble report rate for any given wire center exceeds twice the statewide standard of 1.4 for three consecutive months, FairPoint has agreed to develop a remediation plan to address the issues causing the higher trouble rate and present that plan to the Department for its review.[189] To examine the localized problems in more detail, FairPoint has further committed to present an action plan, within 12 months of close, for analysis and remediation of service quality issues for the next or remaining group of wire centers (if any), where the trouble report rates have consistently (for at least three consecutive months) exceeded twice the statewide standard (to the extent there are such additional wire centers not analyzed as part of the earlier action plan presented within six months of close). We accept this condition, although we require that FairPoint file its plan with the Board as well.

FairPoint has also agreed to accept the Department's proposal condition requiring it to assume Verizon's obligations in Docket 6957. In that proceeding, the Board accepted a proposal from the Department and Verizon that required Verizon, in lieu of $6 million in penalties for poor service quality performance, to install facilities to create redundancy in the network. FairPoint also has committed to complete the Verizon service improvement projects not completed prior to close. Finally, FairPoint has agreed to provide the codes that it will use in its new trouble tracking system. As there is no dispute, if we approved the Proposed Transactions, we would adopt these conditions.

> **Prior to conversion, FairPoint shall provide the Department with the codes to be used in the new trouble tracking system to ensure the codes will provide the same information as reported by Verizon, and ensure that the codes map to the Verizon system used as a basis for the report.**
>
> **FairPoint shall track on a monthly basis, Trouble Report Rates and Troubles Not Cleared in 24 Hours by exchange, and ensure that no exchange has a rate on any of these measures that exceeds twice the**

189. Tr. 9/17/07 at 208, 210–11 (Smee).

> **statewide standard. In addition, if the trouble report rate for any given wire center exceeds twice the statewide standard of 1.4 for three consecutive months, FairPoint shall develop a remediation plan to address the issues causing the higher trouble rate and file it with the Board and Department. Within 12 months of closing, FairPoint also shall develop and file with the Board and Department, an action plan for analysis and remediation of service quality issues for wire centers (other than those already addressed) where the trouble report rates have exceeded twice the statewide standard for at least three consecutive months.**
>
> **FairPoint shall perform on all of Verizon's obligations under the settlement in Docket 6957.**
>
> **FairPoint shall complete any of the improvement projects that Verizon has identified to address localized service quality issues if Verizon has not completed those projects by the date the parties close the transactions.**

Labor's proposals would reset certain baseline standards, adopt new standards, and double penalties. Labor also asks that we require that, if FairPoint fails to meet any individual standard for three consecutive years, the Board would conduct an extensive service quality audit to evaluate the reasons for the continuing failures and recommend remedies. FairPoint asserts that these proposals are unsupported by the record. It also points out that the Department's witness characterized them as punitive. Instead, FairPoint seeks to maintain the standards in the existing Plan.

We do not accept Labor's proposed additions at this time, although several of them deserve serious consideration at the time the Board next reviews the SQ Plan. Labor recommends that we double the penalties in the SQ Plan. Certainly, higher penalties would make it more likely that FairPoint would try to meet the service quality standards. But establishing service quality penalties requires us to consider not only the appropriate incentives for a company to comply with the standards, but also whether the penalties are reasonable in light of the standards and the goals. Here, given FairPoint's size, it appears that the penalty amounts are high enough to create a strong incentive for FairPoint to meet the standards; higher penalties may have the effect of becoming punitive rather than creating an incentive.[190] We would reconsider this issue at the time of the next evaluation of the SQ Plan in 2010 should the Proposed Transaction ultimately be approved.

We also do not accept Labor's proposal that we extend the SQ Plan for five years (through 2012), largely because Labor has not put forth any sound reason for doing so. To the contrary, Labor's proposal would have the effect of separating the term of the SQ Plan from that of the Incentive Regulation Plan (which expires in 2010). It would also mean that the SQ Plan would run for seven years without a comprehensive reevaluation. Neither of these outcomes is reasonable. Rather, the SQ Plan should continue to run for the same period as the Incentive Regulation Plan, so that the Board may reconsider the appropriate incentives in a single proceeding.

Labor also asks that we adopt a new performance standard that would lead to compensation points whenever an exchange had either a trouble report rate or a residential repair rate that exceeded the baseline by more than 20%. We do not accept this recommendation for two reasons. First, as we discuss above, we have adopted a condition intended to track localized service quality issues. We expect that this will help identify and correct problems without attaching specific penalties. Second, Labor has not shown that the 20% threshold is reasonable. The service quality standards are calculated on a statewide basis. We would expect some variation from exchange to exchange on many standards. We would need more evidence before we could determine the level of variance that is reasonable for an individual exchange.

We also decline to tighten the service quality standards for calls not answered and residential repair. As to the former, Labor has shown no reason for changing the baseline requiring that FairPoint answer 75% of calls placed to customer service representatives to instead require 80%. The same applies to the proposed change to the residential repair standard where Labor would have us require that Verizon clear 80% of troubles within 24 hours (compared to the present standard of 70%). We would note that Labor's recommended change to the

190. As we discuss above, the penalties do not, however, appear to have created the appropriate incentives for Verizon, given its consistent failure to meet the residential repair standard. Labor's recommendation to double the penalties may be appropriate if FairPoint's acquisition of Verizon does not occur.

residential repair standard may better reflect consumer expectations than does the current standard. However, we have no evidence on the feasibility of requiring FairPoint to meet the tougher repair standard. We will evaluate both standards again at the time we reconsider the SQ Plan in 2010. We would encourage Labor to raise these issues at this time.

Labor's final proposal would have us conduct an extensive service quality audit whenever FairPoint fails to meet an individual standard for three consecutive years. Here, we find that Labor's proposal has some merit. If a company fails to meet a performance standard for three consecutive years, it would suggest that there are particular operational or capital problems that need to be addressed. However, we are unpersuaded that it is necessary for the Board to conduct a full-scale service quality audit. Instead, if we were to approve the Proposed Transaction, we would adopt the following condition.

> **If FairPoint fails to meet the performance baseline for the same service quality standard in three consecutive years, it shall file with the Board and Department an evaluation of the reasons for not meeting that standard and the proposed corrective actions.**

iv. Quality Assurance Plan

To address service quality concerns going forward, the Department also recommends that the Board require FairPoint to file a detailed quality assurance/quality control plan prior to cutover. The Department views this plan as necessary to ensure that FairPoint is prepared to take operational responsibility prior to cutover of systems.

FairPoint agrees that it should provide the Department with information on the topics that would be covered by the plan. Yet, FairPoint considers the plan itself to be unnecessary.[191] Instead, FairPoint has agreed to provide what it calls its Key Performance Indices to the Department.

In light of the on-going service quality issues over the past several years, we agree with the Department that it is appropriate for FairPoint to prepare a quality assurance plan focused solely on service quality issues. Accordingly, if we approved the Proposed Transaction, we would adopt the following condition:

191. FairPoint Brief at 184.

FairPoint shall provide a detailed management plan that addresses quality and service issues before the acquisition is approved. The plan should address the following.

- **Organizational Structure and responsibility**
- **Implementing a regimented approach to the inspection of work**
- **Quality policies and metrics**
- **Process flow – engineering, construction, testing, service provisioning**
- **Reducing error rate**
- **On time completion rate**
- **Training employees**
- **Analysis of data and improvement**

3. Adequate customer service[192]

a. Findings

i. Existing Customer Service

241. Consumer complaints to the Department represent requests by consumers who are dissatisfied with the resolution of their problem by their carrier. They reflect both an underlying complaint and the company's effectiveness at resolving the complaint. Pariseau pf. at 6–7.

242. Over the period from 2002 through 2006, the rate of customer complaints against Verizon has increased. Consumers have experienced increasingly serious problems with Verizon in the areas of repairs, delivery of service and line extensions. Peres reb. pf. at 21; Pariseau pf. at 6–7; Porell reb. pf. at 12.

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192. To some degree, service quality and customer service overlap; both examine the manner in which a company provides service to its customers. In the previous section, we analyzed the service quality of FairPoint. This focuses on the level of service provided to the customer, looking at issues such as how quickly a company provides service, fixes problems, and initiates responses to consumer inquiries. By contrast, customer service looks at how well a company responds to consumer inquiries and complaints. One measure of the adequacy is the rate of complaints to the Department, which reflects customers who were dissatisfied with the company's response to their problem. Customer service also generally considers the billing issues.

243. The most dramatic increase in consumer complaints against Verizon has come in the area of repair, where complaints jumped over 100% in the period of 2002 through 2006. Pariseau pf. at 7.

ii. FairPoint's Experience in Northern New England

244. FairPoint Vermont's current handling of consumer complaints in Vermont has been adequate, but it still requires, at a minimum, additional training, tighter controls over procedures, improvement in systems and additional staffing. Pariseau pf. at 11.

245. During the period 2002 through 2006, the rate of consumer complaints to the Department from FairPoint Vermont customers has shown a pattern similar to Verizon's, increasing from 3.46 per 1000 customers to 7.14 per 1000 customers. In particular, billing complaints have seen a 200% increase, delivery of service has seen a 500% increase, and repairs have seen a 200% increase. Pariseau pf. at 10.

246. The Department's Consumer Affairs Division currently has three complaints under investigation concerning FairPoint Vermont's billing. The number of open complaints examining FairPoint Vermont's billing is, at this time, almost equal to the number of total complaints received in the entire 2001 and 2003 calendar years. Pariseau sur. pf. at 17.

247. FairPoint Vermont has made efforts to improve its customer service, but it has not provided a high level of service to the consumers of Vermont. Pariseau pf. at 12.

248. In six of the last seven years, FairPoint Vermont had the highest rate of complaints of Vermont's ten local exchange companies – including Verizon. Peres pf. at 8.

249. FairPoint Vermont undertook billing conversions in 2005 and 2006. During both billing conversions, Local Measured Service ("LMS") billing was a persistent problem. Among other problems, some bills did not provide a breakdown of LMS or contained duplicate billing for LMS charges or consumers were charged at an incorrect rate for the LMS charges. Pariseau pf. at 6–12; exh. DPS-TSP-5; Pariseau sur. pf. at 15–17.

250. FairPoint Vermont's latest billing conversion led to an increase in billing-related complaints, in part because of FairPoint Vermont's inability to identify and remedy the underlying causes of the billing errors. Pariseau sur. pf. at 15.

251. During the billing conversions, FairPoint Vermont was not equipped to deal with the number of issues that arose as witnessed by the excessively long wait times experienced by consumers attempting to contact FairPoint Vermont. Pariseau pf. at 9–10.

252. When customer service and service quality issues have arisen in Vermont, FairPoint Vermont has worked with the Department toward resolving the issues. Campbell pf. at 21–22.

253. FairPoint's Maine subsidiaries have also experienced high consumer complaint rates. Peres pf. at 9.

254. In 2006, FairPoint converted the Maine properties to a different system. The conversion resulted in less than acceptable billing accuracy over an extended period of time which created unacceptably high call wait times in the billing center. Nixon pf. at 26; Mills pf. at 9; tr. 9/19/07 at 45–51 (Haga).

255. During the time of billing inaccuracies in Maine, FairPoint stayed in contact with the Maine PUC's Consumer Assistance Division Director to keep him informed as the billing conversion and cleanup progressed. Nixon pf. at 26.

256. Through additional informal meetings with the Maine PUC, FairPoint agreed to submit monthly reports, beginning in March 2006, to document progress in three specific areas: Call Center Performance; Billing Performance; and Accuracy of E911 records. Nixon pf. at 26.

257. Since the conversion, FairPoint has met the Maine PUC's benchmarks. Nixon pf. at 26.

iii. FairPoint's Ability to Meet Customer Service Obligations

258. FairPoint's South China, Maine call center will receive on-going improvements and will continue to support FairPoint's existing operations. Nixon pf. at 5; Leach pf. at 12–13.

259. In addition, FairPoint will open at least three new in-region work centers—a network operations center, an information systems center and an administrative center. Leach pf. at 12–13; Nixon pf. at 15; Nixon reb. pf. at 18.

260. Once completed, FairPoint's conversion of Verizon's back-office systems would likely be a positive development for FairPoint customers. Tr. 9/19/07 at 165–66 (Mills).

261. FairPoint will assume the customer protection and service obligations of Verizon under the SQ Plan. Nixon pf. at 25.

262. FairPoint will have in-market staff to support its business customers and account representatives to meet at customer locations for its medium and large business accounts. Nixon reb. pf. at 5; tr. 9/7/07 at 265 (Lippold); Lippold reb. pf. at 10–11.

263. FairPoint has agreed to have the head of its operations team meet with representatives of the Department on no less than a semi-annual basis to discuss any service quality or customer service issues that have arisen. Tr. 9/20/07 at 153, 156 (Nixon).

264. FairPoint also agreed to meet periodically with officials from the Department on an as-needed basis. Tr. 9/20/07 at 156 (Nixon).

265. FairPoint will have to address service quality issues while absorbing outside plant staff and creating new policies and procedures. At the same time, FairPoint will be expanding DSL service in the Verizon territory. This effort places an extra burden on the newly acquired supervisors and first level managers who must manage daily operations, DSL expansion projects and improve service quality. Wierson pf. at 9–10.

266. The financial penalty provisions of the SQ Plan will serve as a significant incentive to meet state standards for customer service. Tr. 9/21/07 at 14–15 (Nixon); Lafferty pf. at 19–20; tr. 9/21/07 at 106 (Wheaton).

b. Discussion

FairPoint asserts that it intends to provide high-quality customer service. It notes that it has maintained a high level of customer service in its existing territories and that (as discussed in the previous section) it has the capability to provide such service in Vermont. In addition, FairPoint contends that it has made a number of commitments that will improve customer service. These commitments include its agreement to be regulated under the SQ Plan and the PAP, its plan to locate more of its senior managers in Vermont and northern New England, its plan to add personnel and at least three new in-region work centers, and its agreement to hold regular meetings with the Department.[193] Finally, FairPoint maintains that Labor's concerns about FairPoint's existing customer service are unsupported by the record. In this context,

193. FairPoint asserts that it has worked with the Department successfully in the past to successfully address such concerns.

FairPoint also requests that we assign no weight to Labor's survey that indicated the potential loss of many skilled employees.[194]

By contrast, the Department expresses "significant concerns" about FairPoint's customer service track record in the past in Vermont, and in particular with the level of complaints. In particular, the Department cites the experience with FairPoint Vermont's 2005 and 2006 system conversions, which led to an increase in the number of consumer complaints and exposed challenges that FairPoint had either not anticipated or was not equipped to handle. The Department acknowledges that FairPoint has made efforts to improve its customer service. However, based on FairPoint's past level of performance in Vermont, the Department remains concerned about FairPoint's ability to improve customer service while undergoing a systems conversion on a much larger scale than the two previous conversions, occurring in 2005 and 2006. As a result, the Department recommends two conditions designed to protect customers from the negative consequences of the system conversions.[195]

Labor raises the same concerns that it did with respect to service quality. In addition, Labor argues that FairPoint has not demonstrated a commitment to consistently good customer service, citing the high rate of consumer complaints. Labor does not, however, recommend any specific conditions to address its customer service concerns.

The evidence indicates that both Verizon and FairPoint Vermont have experienced increases in the number of customer complaints to the Department over the past several years. The numbers of complaints remain small in absolute numbers, but the increasing rate raises

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194. We addressed this issue in the previous section.

195. The two conditions would (1) hold customers harmless for billing errors resulting from the conversion, including not collecting any under-billing (Condition 23) and (2) providing a bill accuracy guarantee, under which FairPoint would provide a $5 credit each month the bill is inaccurate (Condition 24). As both of these proposals are intended to address concerns with the transfer from Verizon to FairPoint systems, we discuss them below as part of our analysis of transition issues.

questions as to companies' abilities to address customer concerns.[196] Moreover, FairPoint Vermont's rate of complaints outpaces that of all other ILECs in Vermont.

We are also troubled by the fact that several of the concerns about FairPoint's existing operations are directly related to system conversion. When FairPoint subsidiaries in Maine and Vermont changed systems, both ran into problems, leading to a rise in customer complaints. In large part, we address our concerns about the transition from Verizon to FairPoint below, in our discussion of the cutover. Of significance for customer service following the acquisition is the fact that FairPoint did not seem to be equipped to handle the volume of complaints that arose in those previous conversions.[197] Particularly after the first conversion ran into troubles that engendered an increase in complaint rates, we would expect that FairPoint would have made adjustments to its customer service before subsequent conversions. To its credit, FairPoint worked with regulators in each instance to resolve the complaints and resolve the underlying problem.

Although we have some concerns about FairPoint's ability to provide timely and responsive customer service, we find that FairPoint has demonstrated that it is likely to meet this standard, and would deliver better, and adequate, performance. FairPoint will improve its call center in Maine, which now serves FairPoint properties in northern New England, while maintaining other facilities.[198] FairPoint will also open at least three new in-region work centers—a network operations center, an information systems center and an administrative center.[199] FairPoint is hiring additional staff; we do not know how many of these will be assigned to customer service functions, but any additions should help it to respond to customer concerns.[200] In addition, FairPoint plans to locate more of its senior managers in northern New England. These enhancements should enable FairPoint to meet its customer service obligations.

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196. Customer complaints to the Department represent an imprecise measure of a company's performance. They include both valid complaints about a company's performance as well as invalid ones. The absolute number of complaints also does not fully inform the Board as to how many concerns exist as many customers do not raise complaints to the Department. Nonetheless, the change in these figures over time is relevant and raises questions about a company's responsiveness.

197. Pariseau pf. at 9–10.

198. Nixon pf. at 5; Leach pf. at 12–13; tr. 9/19/07 at 165–66 (Mills).

199. Leach pf. at 12–13; Nixon pf. at 15; Nixon reb. pf. at 18.

200. Leach pf. at 12.

FairPoint has also expressed a willingness to work regularly with the Department to address customer service issues.

We also expect that, considering FairPoint's past experiences with system conversions, it will be prepared to address customers' complaints about any new billing or service issues that arise as a result of cutover. As we discuss below, FairPoint presented extensive evidence that suggests that it is well-positioned to minimize system conversion issues. However, the past experience in the FairPoint Vermont and Maine conversions, as well as the experiences of other companies during a major system conversion in Hawaii, suggest that unanticipated problems are possible, if not likely. FairPoint must adequately staff its customer service centers to deal with these potential outcomes.

4. Availability of Emergency services

a. Findings

267. FairPoint's provision of emergency services, primarily Enhanced 911 ("E911") services, is expected to be equivalent to that provided by Verizon. Campbell pf. at 8; findings 268–276, below.

268. At closing, FairPoint will assume ownership and operational control of Verizon's present network in Vermont. FairPoint will also take over the provision of E911 transport connectivity services. Harrington/Brown/Smee reb. pf. at 15; Nixon pf. at 9; Campbell pf. at 8.

269. FairPoint intends to provide voice communications transport and switching from the various Class 5 End Offices through the two E911 tandems located in the state and to the State of Vermont's selective router and Public Safety Answering Point facilities. Harrington/Brown/Smee reb. pf. at 15–16.

270. There will be no change for any service provider external to Verizon and FairPoint. The only change for the properties that FairPoint will be acquiring will be that FairPoint's service order updates will need to be communicated to the State of Vermont's ALI database provider instead of Verizon's service order updates; that change will take place at cutover. Harrington/Brown/Smee reb. pf. at 16.

271. Because FairPoint will use the same network, most aspects of E911 provisioning are unlikely to change. Campbell pf. at 8.

272. Until the cutover, Verizon will continue to provide all E911 services under the TSA. Harrington/Brown/Smee reb. pf. at 16.

273. Under the proposal, FairPoint will acquire the systems needed to interface with the E911 system in Vermont. FairPoint plans to develop the systems to monitor these interactions. Harrington/Brown/Smee reb. pf. at 16.

274. FairPoint plans to test the E911 updates it provides as well as the E911 system and its processes. Tr. 9/19/07 at 58 (Haga, Kurtz).

275. FairPoint will develop an Emergency Response/Restoration plan to address emergencies such as natural disasters; the plan will include arrangements with vendors, other FairPoint employees, employees of other telecommunications companies, the utility companies and contract firms (subject to the provisions of the Collective Bargaining Agreement). Nixon reb. pf. at 26.

276. FairPoint has fewer resources available to respond to emergencies than does Verizon. In the event of a widespread emergency or natural disaster, some additional resources are likely to be available from other FairPoint companies and through the Telephone Association of New England Emergency Resource Book, although these may still be fewer resources than Verizon would have. Campbell pf. at 9; Campbell sur. pf. at 40.

b. Discussion

FairPoint asserts that its acquisition of Verizon's local exchange and long distance businesses will not affect emergency services. According to FairPoint, the state of Vermont operates the E911 system, including its own E911 ALI database and the infrastructure that connects the Verizon system to the E911 database (in contrast to the structure in the other northern New England states). This means that the only change that will occur as a result of the transfer is that FairPoint will, in the future, transfer service order updates to the E911 administrator instead of Verizon.

The Department argues that, although the petitioners have not specifically demonstrated that emergency services would be available, because the transaction essentially will be a transfer of control of Verizon's network in Vermont to FairPoint, it is reasonable to expect that most aspects of Verizon's provisioning of Enhanced 911 service would not change. The Department raises two concerns, however. First, the Department notes the potential for disruptions or errors in the provisioning of information to Vermont's E911 system because of the transition from legacy Verizon systems to the new systems FairPoint will be using after the cutover.[201] Second, the Department contends that FairPoint may have less ability than does Verizon to restore and continue service in a widespread emergency. This concern arises from the fact that Verizon, as a larger company, has more resources on which to draw in the case of such an emergency. To address this concern, the Department recommends in proposed condition 10 that the Board require FairPoint to demonstrate in a compliance filing six months after closing that it has used best efforts to enter into mutual aid agreements with comparably-sized or larger carriers in case of a natural disaster or other widespread emergency.

We find that, subject to the condition requested by the Department (and agreed to by FairPoint),[202] FairPoint has demonstrated that emergency services are likely to be available to the same extent they are today. The transaction will have no effect on significant portions of the emergency services system in Vermont. This is because the provision of E911 service is largely managed by the Enhanced 911 Board working through a contractor to administer the system.[203] Although Verizon had previously provided database and system administrator functions, it no longer does so. Instead, Verizon's primary role (other than simply operating its telephone network to enable calls to the E911 system) is the provision of unbundled network elements under its Tariff No. 29; this includes the transmission of service order changes on a daily basis.

Under the transaction, FairPoint will be taking over Verizon's existing network and, as explained above in Section V.D.1., will be adopting the same tariffs. As the network will remain the same, it is reasonable to expect that all of the network-related functions will be unchanged.

201. The Department does not recommend any specific conditions to address this concern. DPS Brief at 15.

202. FairPoint Reply Brief at 9 and Attachment 1 at 2; FairPoint Brief at 107, Finding 409.

203. Tr. 9/19/07 at 57–58 (Haga, Kurtz).

We recognize, as the Department has argued, that emergency services can be adversely affected by events that disrupt telephone service generally. Verizon's large size provides it access to substantial resources to address such situations. FairPoint, as a smaller company, may not have similar resources available. The condition proposed by the Department — requiring FairPoint to use its best efforts to reach mutual aid agreements with other carriers — should help address any potential harm arising from the fewer resources that FairPoint would have readily available. FairPoint has agreed to this condition, which we would adopt if we approve the Proposed Transaction.

> **No later than six months after closing, FairPoint shall file a demonstration that it has used its best efforts to enter into mutual aid agreements with comparably-sized or larger carriers in case of a natural disaster or other widespread emergency and file copies of any agreements that it has entered.**

5. Adequate Facilities

a. Plant Condition, Due Diligence, and Plant Audits

i. Findings of Fact

277. Through this transaction, FairPoint is acquiring Verizon's switched and special access lines in Vermont, New Hampshire and Maine, as well as its Internet service, enterprise voice services, CPE accounts, and long-distance voice and private line customer accounts (for customer private lines with beginning and end points within the three states) that Verizon served in the region before the 2006 merger with MCI, Inc. Leach pf. at 15–16.

278. There are 8 central office switches and 77 remote switches in Vermont. Verizon's switching network in Vermont is generally robust and efficient. It has the capacity to serve around 500,000 lines, and it currently serves approximately 320,000 lines. Harrington pf. at 5; tr. 9/17/07 at 201 (Smee, Brown Harrington).

279. The interoffice network being transferred includes 110 fiber routes and 40 copper routes. These routes contain nearly 650 trunk groups. Harrington pf. at 5.

280. Verizon's current outside plant in Vermont consists of over 21,000 route-miles of cable. 19,000 miles are copper cable and 2,000 miles are fiber-optic cable. Harrington pf. at 6.

281. Verizon's existing network is designed for voice communications; over time FairPoint will install a data-centric network that is specifically designed for broadband or data services and will be a more robust and redundant network and ultimately cheaper to operate. Tr. 9/17/07 at 225–226 (Brown).

282. FairPoint has developed a Broadband Plan in support of its proposed network-facilities deployment and has budgeted $18,550,000 to complete the plan. Brown/Harrington/Smee reb. pf. at 23.

283. FairPoint will also undertake a substantial, network-facilities expansion to increase broadband addressability to up to 88% of Verizon customers by the end of 2010. Exh. HBS-1.

284. FairPoint has received data on Verizon's Vermont vehicles. This includes the make, model, year, serial number and mileage. FairPoint believes the fleet is in need of remediation. FairPoint plans to and has budgeted to replace 18 of the trucks immediately and will replace more if necessary. Tr. 9/18/07 at 34–35 (Smee); tr. 9/6/07 at 108 (Leach).

285. Verizon has 286 vehicles in Vermont. Of these, 52 have more than 150,000 miles. Tr. 9/18/07 at 34 (Smee).

286. FairPoint has not visited any of the garages where vehicles are kept. Tr. 9/18/07 at 35 (Smee).

287. Following transfers of rural telephone property to new owners, it is often the case that properties that were sold by Bell companies are found to be less adequate than properties that were sold by independent operators. Tr. 9/7/07 at 95 (Balhoff).

288. One risk for FairPoint is that newly deployed DSL overlay systems will either under-perform or require additional capital to extend fiber and add new remote terminal cabinets. For example, copper loops with load coils (this is typically loops in excess of 15k ft. in length) may need to be removed to carry ADSL signals. If the load coils are removed, traditional voice services must be provided over the DSL transport. Wierson pf. at 23–24.

289. These risks could affect both capital budgets and deployment schedules. The cost and schedule impact could be significant depending on the actual copper plant loop profile. Deployment schedules could easily double with the discovery of non-favorable cable data. Moreover, a more thorough knowledge of the Verizon copper plant could lead to alternate

technologies or serving areas. A case in point is the unknown amount of fiber needed to build out the network. FairPoint had identified 44 miles of fiber that must be built and has indicated that 90% of this would be aerial fiber. This alone could cost around $60k per mile (or more) or $2.6M. FairPoint might not be able to meet its service level commitments if additional fiber is required to complete plans to improve the reliability of the network. Wierson pf. at 24–25.

290. The estimated average capital cost of FairPoint's initially-proposed broadband expansion is $169 per additional addressable line. Wierson pf. at 26.

291. Using per line deployment cost estimates from a California Public Utilities Commission Broadband report, the cost per line is somewhere between $700 for reaching 75% of the unserved population and $1300 for reaching 100% penetration per connected line including equipment, deployment costs, core network, and outside plant. Wierson pf. at 26.

292. Normally a telephone company buyer will conduct a spot audit of plant prior to purchase. This entails performing a random audit of one or more of each type of facility in a network selected at random by the buyer. Usually this audit consists of a site survey where the actual configuration is compared to the documentation provided by the seller. The general condition of the network is also evaluated. Repair records especially on items needing periodic maintenance are audited as well. This is done for various Point-of-Presences (POPs) and on the copper and fiber facilities also. The buyer should be allowed to randomly select what they want to audit. Wierson pf. at 10, 23; Wierson sur. pf. at 3.

293. FairPoint began its due diligence process with visits to data rooms to review documentation regarding the assets to be acquired and later moves on to site visits and perhaps data requests. This allowed FairPoint to make reasonable estimates of what the capital costs and operating expenditures were going to be. Tr. 9/18/07 at 56–59 (Harrington); *see* Harrington pf. at 4–5; Brown/Harrington/Smee reb. pf. at 5–13; tr. 9/17/07 at 199–202 (Brown, Harrington); tr. 9/18/07 at 7–9, 28–31, 55 (Brown).

294. FairPoint has reviewed all aspects of the network assets to be transferred with the transaction, including relevant central office, outside plant, and general support assets. FairPoint reviewed extensive documentation relating to Verizon's network in Vermont, including maps, switch data, switch/network elements, detail on subscriber carrier equipment and loop systems,

trouble indices, capital expenditure history, data regarding working and installed trunks, and information about Verizon's E911 network. Harrington pf. at 4.

295. FairPoint conducted several trips with the purpose of physically inspecting, on a sample basis, Verizon's central office equipment, outside plant, and buildings. Harrington pf. at 4.

296. Regarding central office equipment, FairPoint conducted limited visual inspections in Burlington, Montpelier and White River Junction. These 3 sites were chosen by Verizon, based on criteria provided by FairPoint, from among the 85 central office sites in Vermont. Verizon knew in advance when FairPoint was planning to visit. FairPoint also visited 7 central office sites in New Hampshire and Maine. In Vermont, FairPoint found the building conditions to be acceptable. Main distribution frames were very neat and clean. The equipment labeling was consistent and complete for purposes of bar coding and inventory systems. The STPs were located in separate rooms, with strict controlled access to these rooms. In general, FairPoint did not observe anything seriously out of order in Vermont. Harrington/Brown/Smee reb. pf. at 7–9; tr. 9/17/07 at 201 (Harrington).

297. In inspecting the remote terminal sites, FairPoint conducted an outside visual inspection, but did not perform any internal visual inspection. Tr. 9/17/07 at 200–202 (Smee, Brown Harrington).

298. Regarding outside plant facilities, FairPoint reviewed eight conditions at 13 Vermont sites. The conditions examined were: (1) lashing wire breaking or broken at locations; (2) mid-span closures because that normally indicates bad cable sections; (3) multiple cables on the same strand because that normally causes maintenance challenges; (4) extended closures, because that can indicate deteriorating cable at terminals; (5) rotten or deteriorated poles; (6) fiber slack not properly framed or insufficient slack loops; (7) the need for heavy tree trimming; and (8) pole transfer work. The inspection revealed that a majority of the work to be completed after closing involves only simple maintenance; the cable was in good shape, although some cable is in need of maintenance, and some should be targeted for replacement. Harrington/Brown/Smee reb. pf. at 6–7; tr. 9/18/07 at 37–38 (Brown).

299. FairPoint has not physically examined any of the copper infrastructure where Verizon has not implemented DSL service. Tr. 9/17/07 at 211 (Brown).

300. At closing, FairPoint will obtain from Verizon the engineers and other work force it needs to assess detailed data concerning the network. Tr. 9/17/07 at 212–213 (Smee); tr. 9/18/07 at 41–44 (Smee).

301. Based on its due diligence work, FairPoint has concluded that the Verizon network in Vermont is typical of the networks that FairPoint has acquired in the past (although larger) and overall remains in good condition, requiring mainly post-closing maintenance. FairPoint expresses confidence that this network will allow it to provide high quality communication services. FairPoint is "comfortable" with the condition of the inside plant equipment that will be transferred to FairPoint. Also, FairPoint believes that Verizon's low network trouble report supports the conclusion that Verizon's plant is "solid." Nixon reb. pf. at 6; Harrington/Brown/Smee reb. pf. at 9–11; tr. 9/17/07 at 204–205 (Harrington); tr. 9/17/07 at 216 (Smee); tr. 9/18/07 at 56–59 (Harrington).

302. FairPoint recognizes that there are certain areas of the Verizon network that will require repair, maintenance and preventive maintenance work and it has budgeted for completion of that work. Brown/Harrington/Smee reb. pf. at 11–13; tr. 9/18/07 at 37–39 (Brown, Smee).

303. As FairPoint continues to gain a higher level of detail from Verizon, including the knowledge it will gain from the work force after close, it will identify and build a plan for any localities where a focused rehabilitation of the plant will reduce the volumes of troubles and thus relieve stress on the I&M forces in their efforts to restore service quickly on the fewer troubles which are reported. Harrington/Brown/Smee reb. pf. at 14; tr. 9/17/07 at 211–213 (Smee).

304. From trouble reports, FairPoint can identify the source of some maintenance issues and determine whether it is the inside plant, the outside plant, a particular exchange area, or along certain leads. This would allow FairPoint to address maintenance problems affecting service quality. FairPoint plans to use "back office" employees to perform "root cause" analyses of network problems. FairPoint anticipates improving the effectiveness of the outside plant force. Harrington/Brown/Smee reb. pf. at 11; tr. 9/18/07 at 42 (Smee).

305. FairPoint contracted with an outside company to assess the Verizon network, including a portion of the outside plant condition, alarm history and outstanding alarms being generated by the network. Wierson pf. at 10, 22.

306. FairPoint has not examined all sources of data available regarding Verizon's outside plant network. Wierson pf. at 22–26; Wierson sur. pf. at 3–5.

307. Service quality issues that Verizon has been experiencing could be due to the condition of its fiber, copper, and power plant. A plant audit could identify the need for significant investment in upgrades, replacement and/or repair. Wierson pf. at 11, 23–24. Wierson sur. pf. at 4 and 7.

308. An audit of physical plant can reveal service-affecting issues. For example, the audit can lead to the discovery of an old or unserviced battery plant that needs repair or replacement, or backup generators that require repair or have not gone through the manufacturer's recommended maintenance cycle. Wierson sur. pf. at 7–9.

309. Time and money would be required for an outside plant audit, and this could delay investments at those locations that are already known to need rehabilitation. Tr. 9/17/07 at 214 (Brown).

310. If a plant audit were conducted after the closing, it is unlikely that the information gained thereby would lead to any action by the Board. Rather, FairPoint and the Board would learn more about the kind of network FairPoint is acquiring and where the costs are. FairPoint might change its network deployment plans. Tr. 9/21/07 at 70–72 (Wierson).

311. Verizon currently has approximately 175 splice service technicians and 47 outside plant technicians working in Vermont. Therefore Verizon has approximately 222 outside plant employees. This number needs to be increased, and FairPoint intends to hire six additional splice technicians. Tr. 9/18/07 at 40–44 (Smee).

ii. Positions of the Parties

In condition number 9, the Department recommended that FairPoint be required to conduct two plant audits following closing. The first would be a "spot audit" producing a report to the Board and Department within 3 months of closing. The spot audit would be performed on a very small percentage (less than 5%) of the outside plant, but only in areas where service quality issues dominate and where Verizon has not implemented DSL services.

The Department also recommends a complete outside plant audit within 12 months of closing to catalog the current plant condition and help further determine the root cause of present and potential service affecting problems in the state. A copy of the audit report would be provided to the Board and Department within 60 days, along with a similar action plan to rectify all remaining service issues and plant conditions discovered in the audit. The plan would address how newly discovered service affecting issues will be rectified along with how potential service problems will be circumvented.

FairPoint disagrees with both recommendations, contending that the proposed audits would be time-consuming, costly, and of little incremental benefit. FairPoint contends it needs to focus its resources on remedying the issues that can be readily identified or are known to exist instead of "spending substantial resources and time in its first year of ownership looking under stones for other issues that may or may not exist."[204] FairPoint maintains that it has followed an adequate due diligence process that supports its conclusion that the Verizon network is in generally good condition. It admits that some areas will need maintenance, but it asserts that it has an adequate budget for that work and that conducting an audit could actually delay work at locations already known to need rehabilitation. Moreover, FairPoint notes that the proposed audits would be performed after closing and would be unlikely to lead to subsequent Board action. FairPoint therefore contends that its resources would be better spent, and the customers will be better served, if it can address specific trouble areas evident from a review of network trouble report rates.

Specifically, FairPoint proposes to track network trouble report rates by wire center and offers to make two reports:

- For wire centers where the trouble report rates have consistently (for at least three consecutive months) exceeded twice the statewide standard (but not more than 5% of wire centers), FairPoint would develop root cause analyses and remediation plans and within six months of closing would present an action plan for those wire centers.
- To the extent that more than 5% of wire centers meet the above standard, FairPoint would present a similar report within 12 months of closing for those wire centers.

204. FairPoint Brief at 178.

In addition, FairPoint plans to use its field staff, augmented by some new positions, to focus on preventative maintenance as well as specific work that addresses the service quality criterion that has been most problematic in the past, the Percentage of Residential Troubles Not Cleared in 24 Hours.

iii. Discussion

FairPoint managers and staff have experience in acquisitions and have conducted a due diligence review. They believe that they know enough about the Verizon plant to safely close the deal, although they acknowledge they do not yet know enough to run the business from day to day.[205] However, FairPoint is acquiring a system substantially larger than all of its current operations combined.

We agree with FairPoint's conclusion that many aspects of Verizon's plant are "solid" and perform well. In general, the facilities that FairPoint proposes to acquire are adequate to provide service. However, issues remain and we are not persuaded that FairPoint fully understands all of the possible material deficits in Verizon's plant, particularly the major, and critical, portion between the outside wall of the central office and the customer's premises. The evidence also supports the Department's assertion that FairPoint has not conducted a sufficient review of Verizon's Vermont facilities to understand fully the nature of the facilities and the expenses that are likely to be incurred in taking over the system.[206] FairPoint examined outside plant at a limited number of Vermont sites and did not look inside remote platform cabinets at all.

Second, the pole dispute with Vermont Electric Cooperative, Inc. has been settled (discussed below), but it illustrates how FairPoint's knowledge of outside plant conditions is still maturing in significant ways. Finally, although FairPoint has a budget for replacing vehicles, it did not actually inspect Verizon's vehicle fleet. FairPoint argues that if it encounters unexpected difficulties in this area it can and would replace additional vehicles right away because to do

205. Tr. 9/17/07 at 215 (Smee).

206. Wierson pf. at 22-26.

otherwise would sideline its work force.[207] While this is undoubtedly true, our primary concern is that the vehicle fleet will become just one more source of unexpected costs.

Overall, while FairPoint has conducted a reasonable due diligence process, we are not convinced that it knows the full extent of the facilities problems it faces. Because FairPoint's financial resources are limited, unexpected budget overruns in these areas could materially reduce the probability that FairPoint itself will operate the company consistently with the commitments and obligations arising from this proceeding.

Nevertheless, we also conclude that post-closing audits cannot provide information to this Board that will be material to approval or disapproval. After closing, therefore, we defer to FairPoint's discretion regarding the best way to manage its new facilities, and we decline to impose the Department's recommended post-closing plant audits. The Department has also not shown the value of conducting a plant audit rather than relying on service quality issues, operational experience, and trouble report rates to identify specific problems. This deference is particularly important given FairPoint's concurrent tasks of reducing the frequency of trouble reports not cleared within 24 hours, remediating localized service quality issues, and complying the obligations we are imposing here regarding double pole removal.

In reaching this conclusion, we rely, in part on FairPoint's agreements (addressed above in the service quality discussion, Part V.C.2.) relating to tracking and remediation of localized service quality issues. FairPoint's assessment of trouble report rates at the wire center level is a significant enhancement to Verizon's current practice, and can produce detailed information that would be useful both to FairPoint and, if FairPoint cannot maintain service quality, to this Board.

b. Pole-Related Issues

i. Findings of Fact

312. Verizon and electric utilities have inter-company agreements in place that address a variety of joint operations issues. One area of the agreement addresses pole setting territories. Utilities share the responsibility of setting poles and then both attach to it in accordance with their agreement. Mertens pf. at 2.

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207. Tr. 9/18/07 at 36 (Smee).

313. When customers seek service from Verizon and the work involves Verizon setting new poles, it has been common for the work to take as long as six months to be completed. Since electric utilities rely on attaching to the same pole that Verizon sets for its use, this sometimes causes long delays before customers can receive basic services. Mertens pf. at 2.

314. During emergencies and storm restoration, pole-owners have the first responsibility to repair or replace damaged facilities. In the past where Verizon was responsible for damaged poles, Verizon dispatched a crew from a distant "garage," such as from Rutland to White River Junction. This caused long delays before electric and telecom service could be restored. Mertens pf. at 2.

315. FairPoint intends to honor all ownership and maintenance agreements related to poles. Nixon reb. pf. at 34.

316. Although not yet in control of the operation, FairPoint has already undertaken to improve cooperation with electric utilities concerning infrastructure and other matters. Nixon reb. pf. at 38.

(a) Dual Pole Issues

317. Neglect of work on poles is an issue of great concern to municipalities. In numerous cases Verizon has failed to remove its old poles after other utilities had transferred their facilities to the new poles. In such cases, either some facilities remain on each of the dual poles, or the old vacant poles remain as an aesthetic distraction in the neighborhood. Old poles also pose a potential safety hazard. In some towns, utilities have been denied permission to set new poles because of this condition. Mertens pf. at 3.

318. The major non-routine maintenance work needed for the system relates to dual poles and the transfer of Verizon cables from old poles to the new poles. Tr. 9/18/07 at 30 (Brown).

319. FairPoint's due diligence review was not designed to produce reliable information regarding the frequency of double poles and similar pole problems in Vermont. The FairPoint teams inspecting outside plant looked primarily at major routes and were not instructed to sample secondary routes. Tr. 9/18/07 at 28–29 (Brown).

320. FairPoint's visiting teams in some areas noticed poles that had been moved back or had been relocated. The Verizon cables that were left on the old poles would be difficult to move back intact because of insufficient slack, and a work order would be needed to rebuild the route observed by FairPoint. Tr. 9/18/07 at 30 (Brown).

321. In the VEC territory, there are at least 1,500 dual poles, out of a total of more than 40,000 poles. This is approximately 3.8 percent. This ratio is higher in VEC territory than in the territories of other electric utilities. Exh. VEC-1; tr. 9/18/07 at 32 (Smee); tr. 9/20/07 at 64 (Hallquist).

322. In the VEC territory, Verizon has fallen farther behind in pole maintenance work every year since 2000. As a general rule, unless VEC complains about a particular pole, poles do not get removed. Tr. 9/20/07 at 65 (Hallquist).

323. Based on the information FairPoint has gathered in Vermont and New Hampshire, FairPoint estimates that one percent of poles in the region are double poles, but it may be as high as two percent. FairPoint plans to use routine maintenance funds to fix these problems and has not set aside a separate budget for this purpose. Tr. 9/18/07 at 32–33 (Smee); tr. 9/20/07 at 224 (Nixon).

324. The Department convened workshops at the end of 2006 concerning Verizon's practices. The group identified problematic areas and root causes for all the major concerns, and the participants agreed to broad corrective action plans. The initial focus was on resolving (a) line extension delays and (b) improving utility-Agency of Transportation coordination in response to highway projects. However, no inventory or count of double poles was undertaken. Mertens pf. at 2; tr. 9/20/07 at 85 (Mertens).

325. Some double poles have been in place as long as ten years. Tr. 9/20/07 at 85 (Mertens).

326. The backlog for pole removal has created unsightly, obstructive and dangerous conditions in Vermont. Mertens sur. pf. at 2.

327. In addition to reaching an agreement with VEC, FairPoint has contacted Green Mountain Power Corporation, Central Vermont Public Service Corporation and the City of Burlington Electric Department. FairPoint hopes to enter into similar agreements with the other

utilities that will require it to remove all double poles within 42 months of closing. Exh. VEC-1; tr. 9/18/07 at 31–32 (Smee); tr. 9/20/07 at 223, 230 (Nixon).

328. Although the removal of double poles is an important issue, other work can properly take greater priority for outside plant staff, including line extensions, storm restoration and tree trimming. In addition, new poles must be set. Tr. 9/20/07 at 82 (Mertens); tr. 9/20/07 at 177 (Nixon).

329. Based on discussions with Verizon and Vermont electric utilities, FairPoint proposes to remove all double poles within 42 months of closing. This consists of six months for a start-up period and 36 months to complete the work. Tr. 9/20/07 at 176–177, 222–223 (Nixon).

330. FairPoint believes that in its agreement with Verizon, FairPoint assumed the responsibility for removing double poles left behind by Verizon after closing. Tr. 9/20/07 at 226 (Nixon).

331. Verizon has agreements with electric utilities requiring it to remove newly created double poles within 90 days. FairPoint has committed to honor those agreements for all new double poles. Tr. 9/20/07 at 222–223 (Nixon).

332. The cost of removing a double pole can vary greatly, depending on the circumstances. The simplest case is removing a pole that has no facilities on it, and the cost of removing such a pole could be as low as $80, but would probably be higher. A very difficult complex pole removal project might take two days and cost $1,600. Tr. 9/20/07 at 93–94 (Mertens).

333. FairPoint has not made a special budget allocation for double pole removal. Tr. 9/18 at 33 (Smee).

(b) Settlement with Vermont Electric Cooperative

334. FairPoint and VEC have reached a Memorandum of Understanding ("MOU") that resolves various issues related to poles. FairPoint is pursuing similar agreements with the other utilities. Exh. VEC-1; tr. 9/20/07 at 66 (Hallquist); tr. 9/20/07 at 176, 223, 230 (Nixon); tr. 9/18/07 at 31–32 (Smee).

335. The MOU sets forth the agreement of the parties with respect to: communication and coordination of joint pole operations; negotiating a new joint operating agreement and associated

intercompany operating procedures; sharing of easement information; pole inspection and maintenance; a jointly-funded joint pole survey; vegetation management; pole relocations; double poles; new pole sets; conformance with National Electric Safety Code standards; and resolution of disputes. Exh. VEC-1.

336. The MOU provides that FairPoint will eliminate the backlog of approximately 1,500 double poles within 42 months. Exh. VEC-1 at 4.

337. The MOU does not require Board approval, as the parties have agreed to honor the agreement and move forward with the terms contained therein. Tr. 9/20/07 at 51 (Malmquist); exh. VEC-1 at 5.

338. Verizon has recently made progress on one area of dispute: Verizon has been aggressive in correcting past due amounts and resolving those issues. Tr. 9/20/07 at 50 (Hallquist).

(c) Remaining Pole-related Issues

339. FairPoint has committed to develop and maintain a pole inspection program designed so that all jointly-owned poles are inspected initially at or before the age of twenty years and thereafter re-inspected at a maximum of ten year intervals, and proposes that the utility companies maintain their respective existing pole inspection programs. Nixon reb. pf. at 36.

340. FairPoint has committed to work with local electric utility companies to agree on procedures that will permit both FairPoint and the utility companies to respond speedily to emergency pole-replacement situations. Also, within six months of closing, FairPoint has committed to use all commercially reasonable efforts to achieve an average emergency-response time from an initial call report until arrival on scene of the on-call supervisor, technician or repair crew (as required) of not more than two hours. "Major" weather events or weather-related emergencies would require an increased response time. Harrington/Brown/Smee reb. pf. at 38; Nixon reb. pf. at 37.

341. FairPoint has agreed to "globally clarify . . . responsibilities and perform root cause analysis for most of the joint operational problem areas identified during the 2006 workshops between Verizon and the Vermont electric utilities." Nixon reb. pf. at 37.

342. FairPoint generally agrees with the proposed condition that "Joint FairPoint-electric utility protocols for responding during emergencies should be formalized to facilitate timely customer restorations," as FairPoint intends to meet with representatives of utility companies in order to formalize protocols for response during emergencies. Nixon reb. pf. at 37; see Mertens pf. at 4.

343. FairPoint will negotiate with the Vermont Agency of Transportation in good faith with the expectation of reaching an acceptable agreement. Nixon reb. pf. at 38; *see* Mertens pf. at 5.

344. FairPoint will coordinate its work to ensure timely completion of any facilities and pole-related work in response to notices of highway construction, necessary relations and related matters. Harrington/Brown/Smee reb. pf. at 39.

345. FairPoint generally agrees with the proposed condition that "FairPoint must commit to continue to improve inter-company cooperation to maintain landline infrastructure within Vermont; specifically, FairPoint should commit to cooperating with other utilities to jointly operate and maintain poles and making emergency repairs to downed poles." Nixon reb. pf. at 38; *see* Mertens pf. at 1–3.

346. FairPoint will work with the utility companies to identify the locations requiring the movement of wires to new poles and FairPoint will meet with the utility companies to discuss the scheduling of the movement of lines to new poles. Nixon reb. pf. at 38.

347. FairPoint will work with the local utilities to seek arrangements for the utilities to either assist and/or work with the FairPoint teams, including the outside plant construction work forces, to determine if there are alternate ways of deployment to ensure that the work is done in a timely fashion. Harrington/Brown/Smee reb. pf. at 38.

ii. Positions of the Parties

As described in the preceding findings, FairPoint has made a number of commitments addressing pole issues. Generally, FairPoint opposes the imposition of formal conditions, arguing that it would be preferable for it to make bilateral commitments with other utilities, similar to what it has done with the VEC agreement, particularly since other pole-owning utilities are not parties.[208] FairPoint proposes to work with the utility companies to identify locations currently requiring relocation of wires to new poles and to respond promptly when current pole work by other utilities creates new obligations for pole work.

The Department requests detailed conditions covering a number of outside plant issues. The Department contends that Verizon has failed to coordinate properly with various electric utilities regarding their joint ownership and operation of utility poles, and that this has produced a deterioration of service quality and customer complaints. The Department argues that more is needed than coordination and communications among the telecom and electric utilities, because that alone does not guarantee any substantive progress. The Department contends that objective measurement of progress is still necessary, as are appropriate metrics and periodic reporting.[209] Also, the Department recommends continued attention to pole-related issues and a commitment to clear the backlog while implementing improved and effective coordination.[210]

The Department recommends imposing five conditions relating to poles. These detailed recommendations, and FairPoint's responses, are explained in detail below.

VEC requests that we accept the settlement of the pole issues with FairPoint.

iii. Discussion

(a) New Customer Services

In condition number 52, the Department recommends that FairPoint be required to engage its electric utility partners in upgrading response to new customer service requests and pursue improvements in joint operations when filling such requests. To objectively measure the success of these efforts, the Department recommends requiring a tracking report measuring the time required to serve new customers and setting a target goal for good service. FairPoint agrees to this condition and commits to maintain the tracking report as described by the Department.[211]

We appreciate FairPoint's commitment to this important task. We decline to impose the Department's proposed condition, however, because it will be difficult to determine

208. FairPoint Brief at 211.
209. Mertens sur. pf. at 2.
210. Mertens pf. at 4.
211. FairPoint Reply Brief at 17.

unambiguously whether the company has "engaged" other utilities. We do, however, believe that a report documenting progress on FairPoint's commitment is justified. If we were to approve the merger, we would impose the following condition:

> **Within six months of closing, FairPoint shall report on: 1) progress in establishing a tracking system for new customer service requests; 2) whether it has established a goal reflecting good service; 3) the percentage of customer service requests meeting that goal, by month; and 4) a narrative describing improvements that have been made in joint operations with electric utilities when responding to requests for new service.**

(b) Pole Backlog

In condition number 53, the Department recommends that FairPoint be required to inventory all dual poles and establish a "remediation plan" within six months of closing. The Department also would require enhanced communication with municipalities and other utilities to ensure in the future the timely transfer of facilities and pole retirements.

Through its agreement with VEC, Fairpoint has committed to establish such a plan within six months of closing and to describe the quantities of dual poles, their geographic locations, and the work timeline. FairPoint will conduct this work not only in VEC service territory, but throughout its footprint. As part of this commitment, FairPoint will complete this work within thirty-six (36) months of cutover, acting on not less than 500 poles in 2008 and 1,000 poles per calendar year thereafter.[212] This amounts to a promise to complete the work approximately 42 months after closing.

The Department's recommendation and FairPoint's agreement to the VEC settlement are not a sufficient remedy, although we do appreciate FairPoint's willingness to comply. FairPoint properly recommends a systematic inventory of the problem followed by an efficient and organized plan to eliminate the problem. While we agree that FairPoint should have a reasonable time for its inventory work and to develop a plan, the overall time frame is too long. FairPoint has an understandable desire to solve the dual pole problem within the limits of its normal construction resources. However, Verizon's neglect of its pole removal obligations has created

212. FairPoint Reply Brief at 17; tr. 9/20/07 at 230 (Nixon).

unsightly, obstructive and dangerous conditions in Vermont. Forty-two months is far too long to solve a problem that has been going on for many years.

If we were to approve the merger, we would require a more aggressive strategy to solve this problem. First, we would require that the entire task be completed within 12 months following closing.[213] Second, we would allow Verizon to begin work immediately, before FairPoint could reasonably complete an inventory and develop its own plan. Therefore, we would impose the following conditions:

> **All dual poles shall be inventoried and a detailed work plan established within six months of closing.**
>
> **All dual poles existing on the date of closing within Verizon's service area shall be removed by Verizon within 12 months of closing.**

In the context of this condition, a "dual pole" would exist on the date of closing if all utilities but for Verizon have transferred their facilities to a new pole and the old pole remains in place. "Removal" includes all overdue pole maintenance work, including transferring Verizon's existing cables and other facilities to existing new poles and the removal of the old pole.

FairPoint asserts that it has assumed the risk of removing double poles. We recognize that this may be the allocation of responsibility that FairPoint and Verizon have chosen. However, we do not accept it. The responsibility for leaving a large number of double poles in place rests solely with Verizon. Verizon allowed this problem to arise over a number of years when it should have removed the poles in a timely fashion. Having created the problem, the responsibility for remediation must rest with Verizon; FairPoint should not now become responsible for problems arising from Verizon's significant neglect. To permit otherwise would set a dangerous precedent by allowing a utility to leave Vermont after such widespread and longstanding neglect.[214] If a Vermont utility in the future is experiencing reduced revenues and thinks it might have to sell, we do not want to create any incentive to defer outside plant maintenance while the utility seeks to defer the inevitable. This concern is particularly acute where, as here, the selling utility's price substantially exceeds book value, and the buyer's

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213. Because today's decision creates a risk that this merger may not close, we intend to independently open a separate proceeding to establish Verizon's obligations in this area.

214. If the FairPoint merger fails to close, we do not waive any remedies that currently may exist against Verizon.

financial soundness is in issue.[215] Thus, if the Proposed Transaction was approved, we would assign sole responsibility for this work to Verizon and we would not permit Verizon to terminate its businesses in Vermont until the work had been completed.

We acknowledge that, in some cases, it may be reasonable to allow the selling utility to contractually agree with the acquiring utility to perform the remediation. We would only accept such an agreement if the acquiring utility has been fully compensated for performing the remedial work within a timely manner and without any disruption of normal capital and operational expenditures. To our knowledge, that has not occurred here. To the contrary, even though FairPoint has stated that it is responsible for pole removal, it has also testified that it can only feasibly remove the poles over a 42-month period without significantly disrupting other investments, including those for broadband and to remedy service quality issues. Thus, if we approved the proposed arrangement, we would be left with accepting an unreasonably long remediation period or forcing FairPoint to incur additional costs that could further strain its finances.

To ensure that Verizon actually performs the work, we would take two measures. First, we would not allow Verizon's Certificate of Public Good to be revoked until the work had been completed.

Second, we would require Verizon to post an escrow amount to ensure that the work is actually done. The primary responsibility for taking out double poles would remain on Verizon, and Verizon would presumably use its own crews for most or all of the work. The fund would ensure that this work is done within the time allowed. It would be administered, however, by a neutral third party and in a way that would allow Verizon to minimize its own expense by doing the pole removal work itself.

For these reasons, we would require Verizon to establish an Overdue Pole Work Reserve Fund and to deposit cash in that fund before closing. FairPoint would have the right to use this cash to pay the costs of removing double poles which it had given Verizon a reasonable

215. We are particularly concerned that we do not know with any certainty how many double poles exist, and the record provides only rough estimates of the average cost of removing these double poles.

opportunity to remove. The balance of the fund, with interest earned, would be refunded to Verizon when FairPoint certifies that the work is complete.

The record does not offer us a precise basis to calculate the proper size of the reserve fund. We do know that Verizon has 21,000 route miles of cable in Vermont. Making what we believe are conservative assumptions, we estimate that 80 percent of Verizon's plant is aerial plant and that it has 25 poles per mile.[216] We also take what appears to be FairPoint's median assessment of double pole frequency, and assume that one percent of Verizon's poles are overdue for work. That produces an estimated 4,200 poles needing work.

We also know that the cost of removing poles can vary from \$80 to \$1,600. Given the weak record and the need to ensure that the work is done, we select the higher number, and we assume that the average cost of performing overdue pole work will be \$1,600 per pole. This should cause only minimal hardship on Verizon because it can obtain a refund of the entire amount by doing all the work with its own crews. Therefore, the size of the Overdue Pole Work Escrow Fund should be \$6,700,000. In sum, if we were to approve the merger, we would establish the following condition:

> **Before closing, Verizon shall establish an Overdue Pole Work Escrow Fund of \$6,700,000 with a neutral administrator. The fund shall be available to FairPoint to compensate it for costs associated with removing the dual poles, using procedures designed to give Verizon reasonable opportunity to perform pole removal work using its own resources. The balance, with interest, shall be refunded when FairPoint certifies that the work has been completed.**

FairPoint has also committed to develop and maintain a pole inspection program designed for all jointly-owned poles to be inspected initially at or before the age of twenty years and thereafter re-inspected at a maximum of ten year intervals, and proposes that the utility companies maintain their respective existing pole inspection programs. We accept this commitment as an appropriate policy for FairPoint to adopt.

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216. This assumes an average pole spacing of 211 feet.

(c) Emergency Response

In condition number 54, the Department recommends that joint FairPoint-electric utility protocols for responding during emergencies should be formalized to facilitate timely customer restorations. The Department asks that these procedures be mandated to be in place at closing.

FairPoint maintains that it does not have existing relationships with the respective utilities, making it difficult if not impossible to meet the Department's deadline of having these protocols in place at closing. FairPoint commits to engage in a good faith effort to have the requested protocols in place within 12 months of closing, to the extent a utility has requested such protocols.[217] FairPoint also has committed to rigorously adhere to the terms of existing pole agreements and has agreed to work with Vermont utilities to resolve other pole-related issues such as inspection, tree-trimming and emergency pole response procedures.

We accept the preceding commitment as an appropriate policy for FairPoint to adopt, but it does not fully resolve the emergency procedures issue. Such procedures are essential to help ensure timely recovery from any significant events or emergencies. Moreover, FairPoint has not shown any basis for allowing it to take a full year to establish emergency protocols with electric utilities. If we were to approve the merger, we would adopt the Department's recommendation, in the following form:

> **FairPoint shall adopt written emergency protocols for each electric utility in its serving area. The protocols shall be filed at the Board and Department by closing. If possible, the protocols shall be jointly adopted with the relevant electric utility.**

FairPoint has also committed, within six months of closing, to use all commercially reasonable efforts to achieve an average emergency-response time from an initial call report until arrival on scene of the on-call supervisor, technician or repair crew (as required) of not more than two hours. "Major" weather events or weather-related emergencies would require an increased response time. We accept this commitment as an appropriate goal for FairPoint to adopt.

217. FairPoint Reply Brief at 17.

(d) Problem Analysis

In condition number 55, the Department recommends that FairPoint should commit to globally clarifying responsibilities and perform root cause analysis for most of the joint operational problem areas identified during the 2006 workshops between Verizon and the Vermont electric utilities. The Department does not specify what those problems are, but we understand that they amount to joint pole management, in its broadest terms.

FairPoint has agreed to globally clarify responsibilities and perform root cause analysis for most of the joint operational problem areas identified during the 2006 workshops between Verizon and the Vermont electric utilities. However, FairPoint opposes a formal condition.[218]

We accept this FairPoint commitment as an appropriate goal, and we decline to impose the condition recommended by the Department. The principal problem with the condition is that it is of undertermined scope. FairPoint will undoubtedly do some "clarification" of responsibilities and some "root cause" analysis with or without a condition. Even under the best of circumstances, it will be difficult later to determine whether FairPoint adequately complied with such a condition. If there is a continuing problem with FairPoint's pole management, we think it more useful for the Department to reactivate its workshop process and, if that proves inadequate, petition for a Board investigation.

(e) Agency of Transportation

In condition number 56, the Department recommends that FairPoint should develop an acceptable pole attachment agreement with the Vermont Agency of Transportation ("AOT").[219] As to the future, the Department argues that agreements between parties which require action within a certain amount of time, such as 90 days, should be enforced.[220]

FairPoint does not agree that it should be required to comply with such a condition. FairPoint does agree to negotiate in good faith with the AOT and expects to reach a mutually acceptable agreement. However, FairPoint argues that the Board would inappropriately influence

218. FairPoint Brief at 211, 212.

219. Mertens sur. pf. at 3.

220. Tr. 9/20/07 at 80–81 (Mertens).

the process by establishing a condition related to any agreement with the AOT.[221] Since we cannot mandate that negotiations would produce an "acceptable" agreement between FairPoint and AOT, we accept FairPoint's commitment as appropriate, and we decline to impose a condition.

FairPoint also committed to coordinate its work with AOT to ensure timely completion of any facilities and pole-related work in response to notices of highway construction, necessary relations and related matters. We accept this commitment as an appropriate goal.

6. Adequate rate of investment

a. Findings

348. FairPoint projects capital expenditures in the three northern New England states that are below Verizon's absolute dollar level of investment for the last several years. These projected expenses are also below the average annual investment that Verizon has made over the last five years. Leach reb. pf. at 47; Wheaton pf. at 6; Campbell sur. pf. at 33; Campbell pf. at 26.

349. On a per-line basis, FairPoint plans to invest more than Verizon has over the last two years (if Verizon's investment in FIOS is excluded). FairPoint's budget includes monies for additional service personnel, a preventative maintenance program and also includes $18.6 million to substantially expand broadband in Vermont. Leach reb. pf. at 51–52; Harrington/Brown/Smee reb. pf. at 15, 23, 25, 33; Wheaton pf. at 9, 14–15, 21; exh. HBS-1.

350. FairPoint projects that annual recurring capital expenditure levels (absolute dollars) will decline slightly over the projection period; this also reflects FairPoint's expectation of continuing declines in equipment costs due to ongoing improvements in technology. On a per-line basis, FairPoint's capital expenditures will rise. Leach pf. at 29–30; Balhoff reb. pf. at 5–6.

351. In addition to annual capital expenditures, FairPoint plans initial, one-time capital expenditures that will include investments in back-office systems and in-region facilities as part of the FairPoint conversion as well as the initial DSL build-out of $18.6 million. Leach pf. at 30, 31; Leach reb. pf. at 49–52; exh. HBS-1.

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221. FairPoint Reply Brief at 213.

352. FairPoint's ability to fund its capital program is based on projected cash flows, which it projects will be sufficient to cover both capital expenditures and dividend payments. If FairPoint can attain its projected level of free cash flow, it should still have access to equity and debt capital markets if needed to fund capital expenditures. Wheaton pf. at 9 and 15.

353. FairPoint's financial projections reflect the funding of future capital expenditures on a pay-as-you-go basis; that is, all will be funded from internally generated funds and none will be funded by additional borrowing or through the issuance of additional shares of common stock. Wheaton pf. at 14–15.

354. The capital structure and financing arrangements that are in place for the transaction would place no encumbrances on the assets of the three-state operations and would not require a guarantee from the three-state operations. Tr. 9/5/07 at 55 (Leach).

355. FairPoint has committed to reserve a portion of its credit facility to meet operational and capital expenditure requirements in Vermont. Tr. 9/5/07 at 94 (Leach).

356. FairPoint's financial ratios, its improving capital structure, and its size following the merger, means that the capital markets will remain open to it should it need to access them. Leach pf. at 36.

357. The union contract's provision that requires only union employees to install new technology and network facilities may limit, delay or reduce FairPoint's ability to investment in and deploy DSL facilities in Vermont as projected. Wheaton pf. at 8–9.

358. Based upon FairPoint's financial projections, FairPoint's capital expenditure plans are adequate to provide for needed investments to maintain and improve service quality and expand broadband. Leach reb. pf. at 51–52; Harrington/Brown/Smee reb. pf. at 15, 23, 25, 33; Wheaton pf. at 9, 14–15, 21; exh. HBS-1.

359. FairPoint's historical capital expenditure levels indicate that it has invested in its plant at a level consistent with the comparable guideline companies. Similarly, FairPoint projects that the level of its future capital expenditures will also be consistent with and comparable to guideline companies. King reb. pf. at 20–24; Balhoff reb. pf. at 9–12.

360. Capital expenditure levels are shrinking (relative to depreciation) across the telecommunications industry because (1) the number of access lines is shrinking and capital

expenditures in earlier years were accommodating line growth that was 3%–5% (in the 1980s and 1990s) and (2) the price of electronics is falling, which means that replacement technologies are less expensive and more efficient. Balhoff reb. pf. at 11; Leach reb. pf. at 38.

361. Verizon is the only major local carrier whose expenditures exceed its depreciation levels and only because of the historically unprecedented investment in FiOS. FairPoint's ratios of capital expenditures to depreciation are comparable with industry norms. These ratios are rising and are projected to reach 77% by 2015. Balhoff pf. at 8; Balhoff reb. pf. at 9–11; Leach reb. pf. at 46–47.

b. Discussion

FairPoint contends that the evidence demonstrates that its capital budget is adequate to provide services to its ratepayers and to make the contemplated network investment. According to FairPoint, when Verizon's FiOS investments are excluded, FairPoint will be investing more in the northern New England properties than Verizon has spent over the last two years on a per-access line basis. FairPoint also asserts that these investment levels are consistent with those of its peers. These investments, argues FairPoint, will also provide broadband capability superior to that of Verizon. In addition to its normal capital expenditures, FairPoint notes that it will be investing in new, more efficient back-office systems. FairPoint also maintains that it will have continued access to the capital markets to fund capital investments. To provide additional assurances, FairPoint has committed to reserve a portion of its credit facility to meet any unexpected operational and capital expenditure requirements that will apply to Vermont.

The Department argues that FairPoint has not adequately demonstrated that its proposed rate of capital investment in Vermont is adequate. The Department asserts that FairPoint must show more conclusively how its capital expenditure levels are adequate to maintain and improve service quality and expand broadband. In addition, the Department contends that FairPoint has not shown that it will have adequate resources — and will commit those resources — to deal with contingencies requiring additional capital. As a result, the Department has recommended conditions related to the transfer of cash from FairPoint's Vermont operations to the corporate level (these are discussed above in the analysis of FairPoint's financial stability and soundness).

Evaluation of the adequacy of FairPoint's (or any company's) planned investments is a difficult proposition. FairPoint presented little direct evidence on its capital needs (other than the approximately $18 million required for the broadband program). Instead, FairPoint used Verizon's historic capital expenditures as a rough proxy for its future needs. This raises two concerns.

First, it is not clear whether Verizon's expenditure levels over the last several years reflect the going-forward capital needs. As discussed above, Verizon has been unable to meet its service quality standards; much of this failure appears to be related to staffing levels, rather than capital needs. Nonetheless, some of the increase in consumer complaints stems from delays in facilities deployment, suggesting that capital may be an issue.[222] Moreover, as we discussed above, Verizon has left in place a large number of dual poles; this suggests that its outside plant expenditure levels are too small, particularly since FairPoint estimates that it would take over three years to remedy the problem without disrupting capital expenditures, even with an increase in staff. If one accepted FairPoint's comparisons as a reasonable proxy, on an absolute basis, FairPoint's planned annual investment still is not equivalent to, but rather less than the comparable figures for Verizon over the past five years. Some of these changes may be reasonable in light of the declining number of access lines and the fact that this is a declining cost industry. Nonetheless, FairPoint has not shown that investments at a level less than Verizon's will meet all needs of the network.

Second, FairPoint's comparisons to Verizon do not support the conclusions that it will spend more than has Verizon. Rather than comparing all capital investments, FairPoint made several adjustments in deriving an investment-per-line figure.[223] FairPoint excluded Verizon's investment in FiOS from its comparisons, arguing that this was a specialty product that benefitted a limited number of customers.[224] This adjustment, however, fails to reflect the actual capital outlay that Verizon has made, and presumably finds cost-effective, and thereby artificially distorts the comparison. FairPoint's calculations also exclude unbundled network element

222. Pariseau pf. at 8. An increasing number of consumers have complained about long delays in obtaining line extensions, even after they have paid their contribution in aid of construction.

223. Leach reb. pf at 48–49.

224. Balhoff reb. pf. at 6-8; Balhoff pf. at 11, 20.

("UNE") loops from the line counts used to determine the investment per line. As these loops remain part of the network and may require some investment, this adjustment is also invalid.[225]

Thus, a simple comparison of FairPoint's planned capital investment to Verizon's historic figures indicates that FairPoint plans similar, albeit lower, levels of capital investment. But it does not fully demonstrate that these investment levels will meet ongoing needs.

Notwithstanding this concern, we find that, subject to the conditions set out in this Order, FairPoint's rate of investment could be adequate. FairPoint's projections are just that — projections. FairPoint will be subject to the Incentive Regulation Plan, Section IV of which specifically sets out an obligation to maintain adequate investments:

> During the term of the Plan, Verizon shall maintain at all times a level of infrastructure investment and operating expenditures sufficient to maintain the ongoing integrity of its network and the reliability and availability of its services.[226]

This creates an affirmative obligation on FairPoint to devote sufficient capital to the network, even if it exceeds the projected needs. We will continue to monitor FairPoint's adherence to this condition.

In addition, if FairPoint's projections about its capital needs, including the capital to expand broadband in Vermont, and cash flows are accurate, it should have sufficient capital to meet these needs. And, if FairPoint needs additional capital, it should have access to capital markets if it operates in accordance with the financial projections.[227] The assets of the northern New England properties also are unencumbered.[228] This ability to fund needed investments and access capital is, of course, linked to FairPoint's overall financial situation. As we discuss above in Part V.C., we have significant questions as to the assumptions on which FairPoint relied and therefore its ability to sustain the cash flows it projects. For this reason, we could only find that FairPoint will have an adequate rate of investment if FairPoint can fully address our concerns about the overall financial soundness of the post-merger entity.

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225. It is not clear from the testimony whether FairPoint made the adjustment for UNE loops for both Verizon's historical capital expenditures and FairPoint's planned future investment.

226. Dockets 6959/7142, Order of 4/27/06, Appendix A at 5.

227. Leach pf. at 36.

228. Tr. 9/5/07 at 55 (Leach).

7. Compatibility with Other Systems

a. Findings

362. The system will be compatible with neighboring systems and FairPoint will provide the same level of connectivity to other carriers at the same prices and terms as does Verizon. Findings 363–366, below.

363. Verizon's network is currently interconnected with other ILECs and CLECs, IXCs and wireless carriers (both affiliated and non-affiliated) in Vermont. As the largest incumbent LEC in the state, Verizon has deployed a network allowing inter-connection and transport to most parts of the state. Lafferty pf. at 12–13.

364. Seamless interconnection with neighboring telecommunications networks, both incumbent local exchange carriers (ILECs) and competitive local exchange carriers (CLECs), as well as with inter-exchange carriers (IXCs) and wireless carriers is critical to the operation of the public telecommunications network. Therefore, it is essential that FairPoint provide the same level of connectivity to other carriers as did Verizon, using comparable technology and at the same prices and terms. Lafferty pf. at 12–13.

365. In most cases, the Proposed Transaction will not change the compatibility and connectivity of networks and operations with neighboring systems. Lafferty pf. at 13–14.

366. FairPoint will charge the same rates for access and other interconnection services as Verizon. Lafferty pf. at 15–16.

i. Wholesale/CLECs

367. FairPoint will assume Verizon's wholesale tariffs (and Statements of Generally Available Terms and Conditions ("SGAT")); assume or replicate its interconnection agreements and other contracts; and provide interconnection, wholesale services and UNEs to CLECs and other carriers. Nixon pf. at 28; Leach pf. at 8; Lippold reb. pf. at 14; Nixon reb. pf. at 7.

368. If any of the agreements include Verizon operations outside of the three-state Northern New England market (Maine, New Hampshire and Vermont), the agreement may have to be modified by Verizon and FairPoint to segregate the three states. In that case FairPoint has

committed to mirroring the Verizon agreements wherever possible. Nixon pf. at 28–29; Lafferty pf. at 13–14.

369. Because FairPoint will either adopt or put in place mirror interconnection agreements, the acquisition will not change the compatibility of the network and its operations with neighboring systems. Lafferty pf. at 13–14.

370. With FairPoint as the ILEC, wholesale customers should be in at least the same position as they were with Verizon. Lippold reb. pf. at 15.

371. Any changes in the way that wholesale customers interact with FairPoint will be minimal; for wholesale customers that place orders via the web, the only change for wholesale customers will be that they need to visit a new web site and enter a new URL to access the new Wisor system to be installed with cutover. CLEC customers that have seen the Wisor system have said that it is superior to the Verizon system they use today. Tr. 9/18/07 at 149 (Haga); tr. 9/7/07 at 74 (Lippold).

372. FairPoint is in the process of speaking with the wholesale customers that use e-bonding in order to understand their technical specifications; FairPoint does not expect that there will be any hardware or software costs for the wholesale customers because it is using industry standards interfaces recognized by the Alliance for Telecommunications Industry Solutions and is not drastically changing the methods by which the companies communicate. Haga/Kurtze reb. pf. at 41; tr. 9/18/07 at 150 (Haga); tr. 9/19/07 at 61–62 (Haga).

373. The system conversion, which affects all systems that interact with CLECs, is an extremely complex, risky and aggressive system conversion process. Lafferty pf. at 14.

374. Competitors may be forced to incur expenses to adjust their systems to be able to communicate with the new FairPoint systems. Lafferty pf. at 15.

375. FairPoint will communicate all the requirements for interconnection to all other carriers which currently interconnect in any way with Verizon in Vermont. Lippold reb. pf. at 19; Lafferty pf. at 15.

376. FairPoint will provide training sessions, training materials, and a certification process to its wholesale customers at no cost. Lippold reb. pf. at 19.

ii. SS7/STPs

377. The System Signaling 7 ("SS7") network is a fundamental component of local telephony and provides an avenue for all call set up and tear down functionality (with the exception of E911 calling). Wierson pf. at 6.

378. FairPoint will acquire the signal transfer points ("STPs") necessary for service in the acquired territories, including Vermont, as part of the Verizon acquisition. As a result, FairPoint will not need to re-home the Vermont switches. Harrington/Brown/Smee reb. pf. at 18–19; tr. 9/17/07 at 222 (Harrington).

379. Signaling link connectivity to other LECs, CLECs, IXCs, and SS7 signaling trading partners will remain unchanged with the possible exception of adding new Gateway Links to Verizon STP Gateways in Massachusetts and Rhode Island. Harrington/Brown/Smee reb. pf. at 18.

380. FairPoint has contracted with a nationally known SS7 database provider (VeriSign) for E800, LIDB, CNAM and LNP database services; as a result, FairPoint will not be placed in a position of investing in and standing up any signal control points ("SCPs") for those applications. Harrington/Brown/Smee reb. pf. at 18.

381. E911 call set-up and tear-down functionality between Class 5 End Offices and the E911 Tandem switches in Vermont is also controlled by the SS7 network and as a result, there is no exception for E911 calling. Harrington/Brown/Smee reb. pf. at 19.

382. As part of the transition from a Verizon network to a FairPoint one, FairPoint will be required to obtain new point codes, which uniquely identify each Class 5 End Office switch, Access Tandem, STP, and SS7 network-type database, from Telcordia and will need to modify certain translations in the Class 5 Tandem Switches to be acquired from Verizon. Harrington/Brown/Smee reb. pf. at 19–20.

iii. The Independents

383. FairPoint intends to maintain Verizon's existing arrangements with the eight independent LECs and does not intend to increase the cost of or make changes to any services to

be provided to them and their customers. Exh. ITC Cross-1; tr. 9/5/07 at 17–19 (Leach); tr. 9/19/07 at 214–216 (Nixon).

b. Discussion

FairPoint contends that the system it plans to acquire will be compatible with the neighboring systems and will provide the same level of connectivity to other carriers at the same prices and terms Verizon now employs. FairPoint states that connectivity to other carriers will remain unchanged because it will acquire all the elements necessary to operate the SS7 network, including the STPs. FairPoint also plans to maintain existing arrangements and levels of service (including prices) with the Independents. Further, FairPoint asserts that it will provide the same interconnection arrangements for competitors (including both prices and terms and conditions of service), so that those customers will be in at least as good a position than they have been in with Verizon. FairPoint argues that the changes for CLEC customers will be fairly minimal; FairPoint intends to provide training to assist CLECs.

FairPoint also objects to the Department's recommendation that we condition our approval on a requirement that FairPoint compensate interconnecting systems for any costs associated with modifications they must make to interconnect with FairPoint. FairPoint maintains that Verizon makes changes now that require interconnecting systems and customers to alter their systems and operations. Since Verizon does not have to pay compensation now, FairPoint maintains that it should not need to either. In addition, to help minimize any disruptions, FairPoint has committed to reimburse wholesale customers for their pre-cutover expenses (food, lodging, and travel (by car only, up to 150 miles at the IRS rate)) for up to three people per wholesale customer to attend FairPoint-sponsored information or training sessions.

The Department agrees that it is likely that FairPoint's systems will be fully compatible with neighboring systems. However, the Department expressed concern that there is still a risk of serious disruption as FairPoint institutes new systems and switches over to those systems. The Department notes that at the present time, Verizon's network provides a critical means of interconnection between a wide range of telecommunications carriers in Vermont. Because these systems are essential, the Department recommends that the Board specifically require FairPoint to provide interconnection with all neighboring systems in the same manner as Verizon. In addition, the Department contends that if modifications to the method of inter-connection are required, FairPoint should compensate the neighboring system for any costs associated with the modifications required for the neighboring system to interconnect with FairPoint.[229]

We find that FairPoint's systems are likely to be compatible with neighboring systems. In large part, FairPoint will be taking over the existing infrastructure and interconnection arrangements that Verizon now has in place, including the SS7 system used to connect calls. Verizon's system currently interconnects with all of the CLECs operating in the state, as well as IXC and neighboring ILECs; FairPoint's will do the same after the transaction is completed. We are concerned, however, that the transition could produce a period in which FairPoint's system does not interact well with those of other interconnecting carriers. As we discuss in more detail below (in Part V.F.), the cutover of systems presents significant risks. To minimize risks, we find it necessary to adopt the conditions set out in that Part and in the ordering clauses.

We are also concerned about the potential that FairPoint's conversion of its systems could impose additional costs on interconnecting carriers that must alter their systems to maintain effective interconnection. As FairPoint argues, that Verizon periodically makes adjustments to its system and interconnection arrangements that require interconnecting carriers to incur costs of their own. These costs are a normal part of operations for the interconnecting carriers, for which they have not traditionally been compensated. In addition, FairPoint has made efforts to minimize the likelihood of significant cost impacts for interconnecting parties by using industry standards as it develops new systems. We would expect that the costs that CLEC and interconnecting systems may occur to adjust systems will be small, if any, and no different from what they would incur if Verizon made changes. For these reasons, we would not adopt the Department's recommended condition.

We acknowledge, however, that much remains unknown at this time; FairPoint's transition arrangements and the development of entirely new systems have the potential to require interconnecting parties to incur costs to alter their interconnection arrangements that are substantially different in magnitude (to the carrier) from what would be considered the normal

229. The Department recommends that we adopt its proposed Condition 26.

course of business. Thus, if an interconnecting system or CLEC faces costs that are both extraordinary and not consistent with the types of costs to interconnecting carriers arising from the ordinary course of business, a carrier may petition the Board to require FairPoint to compensate them for the atypical expenditures.

E. Likely customer benefits of the transaction

FairPoint contends that it offers four kinds of benefits that should allow us to conclude that granting the petition as a whole will provide a public benefit. Those areas are: (1) planned broadband deployment; (2) improved office systems; (3) economic benefits from greater employment and investment in Vermont; and (4) a new FairPoint economic development program. Each is discussed separately below.

1. Broadband Deployment

a. Positions of the Parties

FairPoint makes several commitments to upgrade broadband availability in Vermont. By adopting Verizon's current broadband commitment under the Incentive Regulation Plan, FairPoint would commit itself to provide DSL to 80 percent coverage of its service area in Vermont by the end of 2010. FairPoint also commits to a specific plan to expand broadband service that should serve "up to" 88 percent of Vermont customers by the end of 2010, notably in the three counties that are currently most under-served. In addition, FairPoint plans to upgrade core network facilities in ways that will provide faster and more efficient DSL services, as well as the possibility of providing fiber-to-the-home facilities in new "greenfield" construction areas.

The Department contends that, even if the Board adopts all of the conditions to protect ratepayers discussed in this Order, FairPoint still has failed to show a public benefit to this transaction. It supports requiring FairPoint to meet the statewide availability commitments required of Verizon through the Incentive Regulation Plan. But, in order to provide a direct benefit to consumers and thereby promote the public good, the Department also asks the Board to impose an additional condition that would require FairPoint, as part of its broadband expansion by 2010, to adopt a "Consistent Coverage Plan." The Department defines "consistent coverage" as providing broadband service, at a speed of not less than 1.5 Mbps per second in at least one direction, to all of the lines served in at least 50% of FairPoint's exchanges.[230] Under the Department's proposal, FairPoint could select which exchanges will receive the 100% coverage.[231]

The Departme nt also questions whether FairPoint's voluntary broadband commitments provide a material improvement over Verizon's current obligations. It characterizes those plans as ambiguous.[232] The Department argues that the claim of 88 percent addressability for DSL by 2010 is unsupported by the record,[233] and that FairPoint has not actually committed to serve a particular number of lines, but only to deploy certain equipment.[234]

Finally, the Department disputes where FairPoint proposes to locate its new broadband facilities. By not following the Consistent Coverage Plan, the Department acknowledges that FairPoint's plan would provide service to some unserved areas, but it also contends that after FairPoint finishes its current broadband deployment, the remaining areas very likely would be even more difficult to reach. According to the Department, this risks "unintentionally complicating the state's planning goal of achieving 100% access."[235] The Department also compares the likely cost of complying with the Consistent Coverage Plan with $32.82 million, the amount of rate reductions that the Board would have required of Verizon in this absence of its commitment to expand the broadband coverage to 80% of its access lines by 2010.[236] The Department concludes that at $700 per line, applied across 40,000 lines, the cost would be less than the foregone rate reductions.[237]

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230. The term "exchanges" refers to the areas that make up the 99 different Verizon rate centers in the state, including localities which are served by central offices in other states. Campbell sur. pf. at 26

231. Procedurally, the Department wants FairPoint to promptly announce which exchanges will have 100% broadband availability. The Department also would constrain FairPoint's selection so that all exchanges targeted for 100% broadband availability would be contiguous with at least one other telephone exchange (served by FairPoint or another company) with actual or planned 100% broadband availability.

232. DPS Brief at 10; DPS Reply Brief at 15.

233. DPS Reply Brief at 14.

234. DPS Reply Brief at 14.

235. DPS Reply Brief at 15.

236. DPS Brief at 103.

237. DPS Brief at 103.

FairPoint opposes the Consistent Coverage Plan, arguing that the plan is unsupported in the record and would result in questionable public policy.

b. Findings

384. FairPoint currently offers broadband to 88 percent of its customers nationally and over 92 percent of its customers in its existing New England territories. Verizon offers broadband services to approximately 62 percent of its northern New England customers. Nixon pf. at 7; Leach pf. at 6; see tr. 9/17/07 at 157 (Porell).

385. FairPoint has submitted, and committed to, a Broadband Plan for the State of Vermont ("FairPoint Broadband Plan") that would increase the addressability of broadband so that up to 88 percent of its Vermont customers would have access by the end of 2010 (34 months after the assumed closing date). FairPoint commits to the plan, and expects that plan to achieve 88 percent addressability, but FairPoint does not commit to that result. Harrington/Brown/Smee reb. pf. at 27 (corrected testimony dated 9/14/07); exh. HBS-1 (confidential); tr. 9/20/07 at 120–128 (Nixon).

386. FairPoint's broadband plan commits it to expend approximately $18.6 million dollars on broadband deployment during the first 24 months following closing. Exh. HBS-1 (confidential).

387. Verizon today provides DSL services using primarily Alcatel-Lucent ASAM technology. Harrington/Brown/Smee reb. pf. at 5.

388. The present technology that Verizon uses is asynchronous transfer mode ("ATM') over a synchronous optical network ("SONET"). The ATM technology approach grew out of the local telecommunications network design in which telephones were connected by "circuits" to a central office. Under this design, once information enters a "circuit," it doesn't exit until it reaches its endpoint, no matter how many "switches" it may traverse. The delivery mechanism in an ATM system is a star-type architecture. All network elements have to come back to a single point where traffic is aggregated. This uses bandwidth inefficiently. Harrington/Brown/Smee reb. pf. at 5, 28–30; Sicker reb. pf. at 6; *see* tr. 9/17/07 at 224–226 (Brown).

389. In the Verizon network, customer data begins as Ethernet Frames (variable size data packets), which are then encapsulated in ATM cells, which are in turn encapsulated into SONET

frames. As a result, 20-30% of the network bandwidth is spent on overhead. It is difficult to conduct intelligent IP network management with this Verizon architecture because the extra layers of encapsulation create extra overhead and because data flows over inefficient routes. Sicker reb. pf. at 22; *see* tr. 9/17/07 at 224–226 (Brown).

390. New DSL network deployments use "IP networking," which uses Internet Protocol ("IP"). Most IP Networking equipment moves larger "chunks" of data, and this leads to higher efficiency. Moreover, the path that data takes through the network is much more flexible than in ATM networks. IP backbone networks can provide performance benefits and cost advantages beyond older ATM telecommunications networks. Sicker reb. pf. at 6–9.

391. The FairPoint Broadband Plan aims first at ensuring that the core (backbone) of the network is sufficiently robust to handle the subsequent build out of edge (or access) technologies. The core backbone will be Internet Protocol/Multiple Protocol Label Switching ("IP/MPLS"). This is a more modern technology than the ATM/SONET technology that Verizon presently has installed in New England, and it will support 10 Gigabit per second data rates. Sicker reb. pf. at 22; Harrington/Brown/Smee reb. pf. at 28–29.

392. FairPoint plans to use a technology called Gigabit Ethernet, which allows Ethernet frames to be more easily routed through the network with less overhead. Ethernet has a 5-6% overhead due to encapsulation, and Gigabit Ethernet can reduce that overhead to 1%. Moreover, IP routers and switches are designed to process Ethernet data directly, making for a more efficient network. Sicker reb. pf. at 22.

393. After first upgrading the core (backbone) of the network, FairPoint will be able to modernize the edge (or last mile) of the network in a way that other carriers using ATM/SONET-based backbone cannot. Sicker reb. pf. at 22.

394. In the second tier of its network, FairPoint plans to make use of Multi-Service Access Nodes ("MSAN") network equipment. This system can support a range of access technologies including basic telephone service, ADSL, VDSL and fiber-to-the-home ("FTTH"). Sicker reb. pf. at 22, 30–32; Harrington/Brown/Smee reb. pf. at 30–31.

395. In serving new DSL customers under the FairPoint Broadband Plan, FairPoint plans to deploy two DSL products. "ADSL2+" supports speeds up to 25 Megabits per second ("Mb/s"),

depending on distance. "VDSL2" supports speeds up to 100 Mb/s, depending upon distance. Sicker reb. pf. at 22, 31; Harrington/Brown/Smee reb. pf. at 30; tr. 9/18/07 at 11 (Brown).

396. FairPoint's ADSL 2+ network will be able to provide access speeds of up to 25 Mb/s up to a distance of approximately 3,000 feet. Tr. 9/18/07 at 11 (Brown).

397. The average FairPoint customer will have the ability to get access speeds of up to 10 Mb/s. Tr. 9/18/07 at 11–12 (Brown).

398. Some of FairPoint's customers will be more than 22,000 feet from a central office or remote terminal. At 22,000 feet, FairPoint expects to be able to provide bandwidth of 1.5 Mb/s. Tr. 9/18/07 at 12, 53 (Brown).

399. Using line conditioning technologies such as "smart coils," FairPoint will be able to provide 768 Kb/s out to 25,000 feet. Tr. 9/18/07 at 12–13 (Brown).

400. At distances of 25,000 feet and beyond, FairPoint looks to alternatives to provide service; in other locations, FairPoint has used pedestal mounted DSLAM units, which will insert the DSL further out in the loop to push access speeds out further, as well as broadband wireless to reach these customers. Tr. 9/18/07 at 14–15, 20, 53 (Brown).

401. MSANs will also allow FairPoint to deploy FTTH for greenfield builds, new businesses and other rebuilds. Sicker reb. pf. at 22, 31; Harrington pf. at 11; tr. 9/18/07 at 59–60 (Harrington).

402. The IP/MPLS network will allow FairPoint to develop and offer advanced broadband services to business, institutional and residential customers that are not supported by the present network architecture. For example, because data is not required to come back to a single aggregation point, if there are different locations along the network such as businesses or schools, FairPoint will be able to build local area network connectivity between multiple points along the network without having to bring all the traffic back to an aggregation point. Sicker reb. pf. at 30; Harrington/Brown/Smee pf. reb. at 29–30; *see* tr. 9/18/07 at 52–53 (Brown).

403. Based on its proposed architecture, FairPoint will better meet the needs of high-capacity broadband customers. Sicker reb. pf. 26, 29–31; tr. 9/20/07 at 186 (Nixon).

404. In addition, the IP/MPLS architecture will support the ability to provide multi-cast services — an IP protocol that allows a single source of signal to be delivered to multiple points

— such as television across Internet protocol, so-called "triple play" options and the transmission of video or audio from one location to other locations such as for business or educational purposes. Harrington/Brown/Smee reb. pf. at 29–30; Sicker reb. pf. at 30; tr. 9/18/07 at 52–53 (Brown); tr. 9/20/07 at 246-47 (Nixon).

405. In other states, FairPoint has successfully designed and implemented IP-based, DSL broadband networks similar in architecture to the network proposed for Vermont. Sicker reb. pf. at 30–31; tr. 9/18/07 at 26–27 (Brown).

406. The FairPoint Broadband Plan is also consistent with the goals expressed in the Department document entitled, Access for All: Meeting Vermont's Broadband and Wireless Goals (February 2007). In particular, the FairPoint Broadband Plan supports the report's goal of providing next-generation networks capable of delivering video, very high speed Internet, and voice with increasing use of fiber optic technology with respect to the core or backbone portions of its network. Sicker reb. pf. at 26–33; exh. FP Cross-15 at 5–6.

407. FairPoint's choice to implement an IP/MPLS, DSL network to deploy broadband to rural Vermont is reasonable within the context of the options available to it, the economics of those options and the rural nature of the Vermont landscape in which FairPoint will operate. Sicker reb. pf. 18–25, 32; *see* Harrington pf. at 9–12; Ileo sur. pf. at 11.

408. Under the Incentive Regulation Plan adopted in Docket Nos. 6959/7142, Verizon is required to make broadband service available to its Vermont customers as follows:

By December 31, 2007:	65% of lines qualified.
By December 31, 2008:	75% of lines qualified.
By December 31, 2009	77% of lines qualified.
By December 31, 2010	80% of lines qualified.

2005-2010 Amended Vermont Incentive Regulation Plan, Appendix A to Docket Nos. 6959/7142, Order of 4/27/06.

409. FairPoint has committed to accepting the obligations of Verizon under the Incentive Regulation Plan, including the broadband deployment obligations. Nixon pf. at 25.

410. Verizon's broadband deployment plan was adopted as an alternative to avoid $32.82 million in Board-ordered rate reductions over the period 2008-2010. Campbell sur. pf. at 23.

411. The FairPoint Broadband Plan is designed to meet and exceed the baseline requirements set forth in the Incentive Regulation Plan. Harrington/Brown/Smee reb. pf. at 26; exh. HBS-1 (confidential); *see* Sicker reb. pf. at 25.

412. The FairPoint Broadband Plan proposes to spend $18,550,000.00 to bring broadband addressability to approximately 88 percent of Vermont access lines by the end of 2010 (within 34 months of closing). Harrington/Brown/Smee reb. pf. at 23, 26; exh. HBS-1 (confidential); tr. 9/20/07 at 120–128 (Nixon).

413. The FairPoint Broadband Plan will proceed in three phases. Harrington/Brown/Smee reb. pf. at 23–27.

414. Phase I will involve the establishment of the core network through the installation of core routers at key locations throughout the state. It will be completed within four to six months after closing, and does not increase the number of customers who can purchase DSL. Harrington/Brown/Smee reb. pf. at 24–25.

415. Phase II will involve the installation of MSAN facilities in central offices that presently do not have broadband services as well as certain other central offices, the installation of approximately 8.8 miles of new interoffice cable between the Tunbridge and Chelsea central offices and power and racking upgrade work to support the new network facilities. Phase II will be executed over a period of approximately 12 months from closing and will bring broadband addressability to an additional 3,927 access lines. Harrington/Brown/Smee reb. pf. at 24–25.

416. During Phase III, FairPoint plans to, among other things, install MSAN units into digital loop carrier sites, lay approximately 57 miles of fiber cable, undertake some fiber splicing and add 200 new digital loop carrier cabinets that presently do not have broadband service and bring them into the network. Phase III is expected to be completed not later than 34 months after closing. FairPoint plans to add 36,762 more broadband-enabled access lines in this phase. Harrington/Brown/Smee reb. pf. at 26.

417. FairPoint estimates that it will reach 75 percent of its customers with DSL addressability within 12 months of closing. Harrington/Brown/Smee reb. pf. at 26.

418. FairPoint has experience in deploying broadband to lower-density areas. Sicker reb. pf. at 29.

419. The standard for acceptable speed for a broadband service is increasing over time. It is possible to take a technology like DSL and push it over long loops, but performance decreases. Campbell sur. pf. at 29–30.

420. 30 V.S.A § 8077 establishes minimum technical service objectives for broadband service in Vermont. It defines broadband as 1.5 Mbps. Campbell sur. pf. at 29–30.

421. The state of Vermont is now committed to a goal of 100% broadband availability. Campbell sur. pf. at 25.

422. FairPoint's collective testimony regarding its broadband commitments is not specific enough to assess whether these commitments are actually an improvement over Verizon's existing obligations. Campbell pf. at 24; tr. 9/21/07 at 178–181(Campbell).

423. FairPoint stated its intent to exceed the level of broadband service availability promised by Verizon. However, a close analysis shows that the size of the commitment is essentially the same, or at least not substantially larger, than Verizon's current obligations. FairPoint has committed to what it characterizes as an acceleration of broadband investment in 2008. However, Verizon is already obliged to reach by the end of 2008 the milestone of 75% of its lines qualified for broadband, up from 56% at the beginning of the plan. Then, over the last two years of its Incentive Regulation Plan, Verizon is obligated to achieve an additional five percentage points of additional broadband availability. Campbell sur. pf. at 11, 17–19; tr. 9/21/07 at 181 (Campbell).

424. The pricing of broadband services under FairPoint's plan will mirror the pricing offered by Verizon today. This will include mirroring Verizon's 3-Megabit service offering. Harrington/Brown/Smee reb. pf. at 32; Campbell sur. pf. at 19; Brown reb. pf. at 28.

425. FairPoint's DSL platform will be at least Verizon's equal and its pricing will mirror Verizon's (at least Verizon's current pricing). However, without a condition, these statements are unenforceable and could change at any time. Campbell sur. pf. at 20.

426. Some exchanges within the state already have 100% DSL coverage. Exchanges operated by some of the independent telephone companies in the state, companies like Waitsfield and Champlain Valley Telecom, Topsham Telephone, and Vermont Telephone, provide 100% broadband availability across their service territories. FairPoint Vermont itself currently provides

100% DSL availability in some of its exchanges, such as Alburgh and Isle La Motte. Campbell sur. pf. at 25–26.

427. In much of Vermont today, broadband service is not available to all customers in the telephone exchange. There are very few regions of the state that are completely without broadband service, but many areas have pockets where service is not available. In many cases, data are estimated about current availability. Campbell sur. pf. at 24, 26; exhs. DPS-CJC-9, DPS-CJC-10.

428. The three most underserved counties in Vermont are Essex (20% DSL availability, 41% total broadband availability), Lamoille (25% DSL availability, 68% total broadband availability) and Orange (33% DSL availability, 62% total broadband availability). The FairPoint Broadband Plan is directed at increasing broadband availability in these underserved counties rather than on areas of the state that do not have broadband DSL service but may have access to broadband via some other medium. Exh. FairPoint HBS-1; exh. FP Cross-14 at 2; Harrington/Brown /Smee reb. pf. at 27 (corrected testimony dated 9/14/07); tr. 9/18/07 at 45–47, 50 (Brown).

429. Under FairPoint's proposed DSL plan, more exchanges will have some DSL, and many exchanges will have more DSL availability. However, the record does not show that any exchanges would have 100 percent coverage. Campbell sur. pf. at 26; exh. DPS-CJC-11.

430. It is more difficult and expensive to reach customers in scattered and discontinuous areas. An existing provider might find it easier to fill gaps in its coverage, but a new provider may need to overbuild already covered areas to reach customers in uncovered areas when the existing pattern of coverage is not consistent. Campbell sur. pf. at 25.

431. DSL deployment in a rural area could cost as much as $700 per line qualified. Campbell sur. pf. at 28.

c. Discussion

Providing broadband Internet access to Vermonters is acknowledged to be fundamental to both FairPoint's business future [238] and to the state's economic health. FairPoint's business plan relies heavily on cash flow, and its management recognizes that deploying broadband widely and

238. Nixon pf. at 7.

effectively will improve FairPoint's long-term financial profitability. We agree with FairPoint that the FairPoint Broadband Plan would provide measurable benefits to Vermont customers in several ways. We accept FairPoint's commitments in these areas, and we would rely on them in reaching any decision to approve the transaction.

First, FairPoint's planned changes to Ethernet and IP formats should provide faster and more reliable service to customers who can purchase the service. By providing 1.5 Megabit service to customers at 22,000 feet from the central office or remote cabinet, FairPoint will provide faster broadband service. The new architecture should also allow for the introduction of new, advanced services to broadband customers, and it will be a benefit to Vermont customers.

Second, FairPoint recently made substantial improvements to its broadband buildout plans. Originally, FairPoint had proposed to spend approximately $13.8 million to bring broadband addressability to up to 80-85 percent of its customers by 2010.[239] Later, FairPoint reworked its plan and significantly increased its proposed spending. FairPoint maintains these changes should bring broadband addressability for "up to" 88 percent of its customers, although it does not commit to achieving that outcome. Moreover, the plan will substantially increase broadband access in the three most underserved counties in Vermont.

Overall, FairPoint's plan has attractive elements. The three-phase buildout plan will provide some speed and availability benefit to Vermonters, and may even be an improvement over any plausible scenario if the merger does not succeed. Nevertheless, as the Department notes, while FairPoint's plan has attractive elements, it does not clearly commit FairPoint to achieving any particular outcomes such as the announced 88 percent coverage level.

The principal question before us therefore is whether the above offerings from FairPoint are sufficient to produce a public benefit for the transaction as a whole, without imposing the added obligations of the Department's proposed "Consistent Coverage Plan." As the Department has cast it, FairPoint would be required to select 50 percent of its exchanges for consistent coverage, but it may select exchanges that best suit its own business interests.

While FairPoint is offering to make a substantial investment in the state, it wants to control the details, by wire center and by neighborhood. The Consistent Coverage Plan would

239. Campbell sur. pf. at 10–23; Harrington/Brown/Smee reb. pf. at 23, 27.

alter this paradigm and instead direct FairPoint to expend some of its capital to serve customers who may not otherwise benefit from the Proposed Transaction and who may not have any alternative source of broadband available to them. Chiefly, FairPoint would be required to apply some of its capital to investments that its management may find likely to be unprofitable or less profitable. FairPoint testified that by requiring it to extend DSL to the last customers found in the edge or "doughnut" areas farthest from the central office, the Consistent Coverage condition would increase FairPoint's average cost. This might force FairPoint to bypass more profitable markets in other exchanges, possibly reducing FairPoint's financial soundness and its ability to compete with other carriers.

On the other hand, the State of Vermont has articulated the legitimate goal of attaining 100 percent broadband service by 2010. The Consistent Coverage requirement would aid the state in meeting that goal. It would aid state government — and in particular, the new Vermont Telecommunications Authority — in meeting its broadband goals. By requiring FairPoint to announce in advance where it will provide ubiquitous service, the state can redirect its time, attention, and resources to other locations.

We also note that the Consistent Coverage requirement is compatible with evolving standards in the telecommunications industry. Most of Vermont's smaller telephone companies have already approached the 100 percent DSL availability standard or have surpassed it. Moreover, FairPoint's own subsidiary in Vermont is providing 100 percent coverage in at least two of its exchanges.[240]

Given the importance of providing broadband service to Vermont's most remote citizens, we accept that the incremental obligation defined by Consistent Coverage as a reasonable addition to the obligations of the state's largest telephone company. We expect, based upon FairPoint's testimony, that this could lead to an increase in costs for FairPoint compared to its financial projections. However, FairPoint presented no evidence showing the magnitude of those

240. The broadband deployment of the Vermont independent telephone companies, including FairPoint, are not directly comparable to those of Verizon. Federal support mechanisms provide greater direct financial incentives for smaller, rural telephone companies to provide broadband service, thus making it much more cost-effective.

costs or whether they would materially affect the financial projections. If we were to approve the merger, we would impose the following condition:

> **While meeting the statewide availability commitments for broadband set out in the Incentive Regulation Plan, FairPoint shall also provide broadband service to all access lines in at least 50% of its exchanges by the end of 2010.**
>
> - **"Broadband" here means a data transmission rate of not less than 1.5 Mbps per second in at least one direction.**
> - **FairPoint shall determine which exchanges it will serve with 100% broadband availability and publicly announce these exchanges as soon as possible after closing. Each exchange shall be contiguous with at least one other exchange (served by FairPoint or another company) with actual or planned 100% broadband availability.**

The current Verizon Incentive Regulation Plan allowed Verizon to avoid a rate reduction in return for making a commitment to provide 80 percent broadband availability by the end of 2010. We approved that settlement, and it binds Verizon and the Department (and, by agreement, FairPoint). The existence of that commitment means that, when considering the benefits of FairPoint's Broadband Plan, we have considered only improvements upon what Verizon has already committed to provide. The obligations that FairPoint is undertaking voluntarily, including its three-phase build-out plan, will provide a benefit to Vermonters. When combined with the obligations of the Consistent Coverage requirement, we conclude that the Proposed Transaction will provide a significant public benefit.

2. Improved Office Systems

a. Positions of the Parties

FairPoint argues that providing "next generation back-office systems" will provide a public benefit to the public because FairPoint systems' architecture will include current technology, utilize some of the latest advances in technology and, over time, allow FairPoint to offer a broader range of products and services.[241]

241. FairPoint Brief at 131; *see* Nixon reb. pf. at 5–6; Haga Kurtze reb. pf. at 43–44.

The Department does not directly contest FairPoint's claim, although it does dispute the value of the new systems. The Department argues in another context that FairPoint places inappropriate weight on new, unproven systems since it is untested as a large telecommunications operator and that its new systems have yet to be proven in production.[242] The Department contends that FairPoint has focused exclusively on its potential success and has not shown forethought on "how it will mitigate the damage to its customers if things do not go according to plan."[243]

b. Findings

432. In connection with the transaction, FairPoint will replace legacy Verizon business, or "back-office," systems with next-generation business systems. The business systems to be replaced include the computer software, hardware and interfaces that are the primary tools used to provide services and products to retail and wholesale customers. Haga pf. at 3–5; Nixon pf. at 23.

433. New systems are likely to better provision existing services as well as potential new services. New systems also offer opportunities to use more current information technology that requires fewer internal data transfers, runs in distributed environments, has the ability to take advantage of continuing technical advances and has broader pools of support personnel. Also, FairPoint may be able to acquire pre-integrated products, thereby reducing the risk of conflicts among separately developed subsystems. Haga/Kurtze reb. pf. at 13–15, 43.

434. FairPoint's replacement of the existing Verizon systems with "state-of-the art next generation applications" will be a positive development for all customers once those systems are up and running. Tr. 9/19/07 at 164–165 (Mills); Mills pf. at 3.

c. Discussion

We address transition issues elsewhere and assume here that they will be successfully addressed. Within that context, we accept FairPoint's assertions that improved back office

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242. DPS Reply Brief at 21; *see* Lafferty pf. at 22; tr. 9/19/07 at 165–166 (Mills).

243. DPS Reply brief at 20–21.

systems will provide a public benefit in Vermont in the form of more efficient and reliable customer service.

3. Employment and Investment in Vermont

a. Positions of the Parties

FairPoint maintains that the acquisition will bring a significant number of new jobs to Vermont, will bring new investment from FairPoint, and will result in a new economic development initiative.

The Department maintains that FairPoint cannot be held to deliver on its promise of increasing employment, and it is therefore not certain that the promised jobs will actually materialize in Vermont, or if they do, how long they will be here.[244] Moreover, the Department notes that FairPoint projects an employment attrition rate of 4 to 4.5% over the next few years. The Department recommends examining only the "leading considerations" which it characterizes as whether FairPoint has the financial, technical and managerial means of achieving essential service quality improvements and more consistent broadband coverage.[245]

b. Findings

435. If the transaction is approved, FairPoint will have approximately 3,500 employees, including newly hired employees. Tr. 9/20/07 at 147–148 (Nixon).

436. FairPoint does not plan to reduce current Vermont staffing immediately as a result of the transaction. FairPoint will not reduce compensation or benefits for the approximately 3,000 Verizon employees, non-union or union, who join FairPoint. They will continue to work at their current locations and in their existing roles. Nixon pf. at 17; Leach pf. at 9.

437. FairPoint will create over 700 new positions in Northern New England. Of those, at least 145 jobs will be in Vermont, primarily in the greater Burlington area. Another 50 new positions will be located in Littleton, New Hampshire. Many of these jobs are call center jobs

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244. DPS Brief at 99.
245. DPS Reply Brief at 32.

that will replace Verizon back-office positions in other states. Nixon reb. pf. at 4, 18–19; Leach pf. at 9.

438. FairPoint's financial model assumes that after 2008 it will reduce employment levels by 4.0 to 4.5 percent per year in Vermont. This is based upon Verizon's historical attrition rate. Exh. Labor-12; tr. 9/5/07 at 182 (Leach)(confidential); tr. 9/19/07 at 7 (agreed to unseal portions of transcript from 9/5/07); tr. 9/20/07 at 200 (Nixon).

439. FairPoint will honor existing collective bargaining agreements until they expire in August 2008. FairPoint is willing to negotiate to extend the current contracts in order to allow time for all parties to implement an orderly transition. Nixon pf. at 17; Leach pf. at 9; Nixon reb. pf. at 14, 30.

440. FairPoint has made a commitment to not reduce employee wages or benefits under the next succeeding contracts. Nixon pf. at 17.

441. FairPoint's initial estimates of compensation levels (in terms of salary, benefit, and related expenditures) are consistent with levels elsewhere in the industry. Ileo sur. pf. at 12.

442. If FairPoint created 195 new positions in and near Vermont and did not decrease other positions, that would boost the State's economy by at least $45 million annually. Ileo sur. pf. at 13–14.

443. Given FairPoint's commitments to maintain Verizon's tariffs, Incentive Regulation Plan, and interconnection agreements, as well as to increase employment in the State, nothing about the transaction will undermine present economic development objectives in Vermont. Ileo sur. pf. at 7.

444. The quality, speed, reliability, and prices of telecommunications services are critical elements in assessing the comparative strengths and weaknesses of localized economies. Deficiencies in available telecommunications services can eliminate a geographic area from a list of potential new business sites, and it can also influence business expansions, relocations, and closings. Ileo sur. pf. at 7–8.

445. FairPoint's capital investment in 2008 is likely to produce incremental capital spending by FairPoint within the Vermont economy of between $20 and $26 million. This should produce an estimated economic effect of between $62 and $79 million of new 2008 goods and services

within the Vermont economy. This analysis assumes: (1) that 50 percent of system conversion capital spent in Vermont will be placed with Vermont businesses; (2) for capital spending which is equivalent to spending that Verizon would make, FairPoint is likely to place an additional amount with Vermont businesses equal to 10% of the capital investments; and (3) the proper multiplier to estimate the overall economic effect of investment in Vermont places with Vermont businesses is 3.0. Ileo reb. pf. at 15; exh. DPS-MJI-3; Ileo answers to Board's written questions on Sept. 13, 2007.

446. For the years 2009–2015, FairPoint is likely to produce incremental capital spending within the Vermont economy of between $3.7 and $5.0 million. This should produce an estimated economic effect of between $11 and $15 million of new goods and services each year within the Vermont economy. This analysis assumes: (1) that 50 percent of system conversion capital spent in Vermont will be placed with Vermont businesses; (2) for capital spending which is equivalent to spending that Verizon would make, FairPoint is likely to place an additional amount with Vermont businesses equal to 10% of the capital investments; and (3) the proper multiplier to estimate the overall economic effect of investment in Vermont places with Vermont businesses is 3.0. Ileo reb. pf. at 15; exh. DPS-MJI-3; Ileo answers to Board's written questions on Sept. 13, 2007.

447. FairPoint is likely to place an additional amount of its capital spending with Vermont businesses equal to 10% of the capital investments. This is based on experience that, as a regional carrier with substantial properties in Northern New England, FairPoint will be likely to place a greater percentage of its goods and services purchases with locally-owned businesses in Vermont than would Verizon, a national carrier. This assumption has been true for other carriers, including United, Continental, Citizens, and GTE. Ileo answers to Board's written questions on Sept. 13, 2007 at 1.

448. These investment projections take into account claims that some of FairPoint's investments will not exceed levels already promised by, or required of, Verizon. They also assume accuracy of FairPoint's estimates for allocating its total capital budget to Vermont. Ileo sur. pf. at 15–16.

c. Discussion

The Department offered testimony seeking to quantify the economic effects of the proposed transfer. This analyzed both employment effects and investment effects.

On employment, the Department estimated the effects of FairPoint's incremental hiring as having a net positive effect of more than $45 million per year on Vermont. However, the Department's analysis did not account for FairPoint's plans to significantly reduce its workforce over time.

We conclude that the transaction will provide a short-term economic boost to the state through higher employment. However, in future years, that benefit seems likely to be reduced or even to disappear altogether if FairPoint reduces its work force in the manner currently planned. For that reason, FairPoint's employment plans will provide a short-term net economic benefit to Vermont. However, we are not able to estimate the long-term economic effect of FairPoint's employment plans because the record is too unclear for us to support such a conclusion.

As to investment, the Department's analysis assumed that FairPoint would be likely to place an additional share of total capital spending with Vermont businesses. This includes both the economic effect of FairPoint's conversion-related expenditures in Vermont as well as the assumption that FairPoint would spend a 10 percent larger portion of its capital investments in Vermont than did Verizon (which had a large non-Vermont component.) While this approaches speculation, his response to our written questions provides at least some support for this assumption, and we accept it.

Based on these assumptions, FairPoint's investment in Vermont appears likely to produce overall benefits to the Vermont economy equal. Under the Department's analysis, these equal between $20 and $26 million in 2008, and between $11 and $15 million per year thereafter. We also recognize a short-term benefit to the Vermont economy from FairPoint's employment plans but we are unable to estimate the long-term economic effect.

4. FairPoint's Economic Development Program

a. Position of the Parties

FairPoint plans to operate a program designed to help communities use technology to spur economic development.[246] FairPoint views this program as a means to advance its own business by moving away from being a supplier of broadband and towards being a generator of demand for broadband services. FairPoint also states that it wants to participate in and to help direct how broadband is used for the betterment of citizens, businesses, and communities.[247]

b. Findings

449. In deploying broadband in Vermont and elsewhere, FairPoint is an infrastructure provider but also seeks to influence how broadband is used. Nixon pf. at 12; tr. 9/21/07 at 10–11 (Nixon).

450. Under FairPoint's proposed Vermont economic development initiative, FairPoint will meet with local communities, regional economic development agencies and state economic development agencies to investigate how broadband can be used to help meet community needs through advance applications. FairPoint is open to considering collaborative relationships with communities and other infrastructure providers. Nixon pf. at 11–13; tr. 9/21/07 at 10–11 (Nixon).

451. FairPoint's economic development initiative will be overseen by the Vice President of Community and Economic Development, a position that will report to FairPoint's President, Peter Nixon. Tr. 9/20/07 at 188-189, 248; exh. PGN-6 (Supp.) at 3.

452. FairPoint's economic development initiative will provide communities with the resources to help them determine their economic needs, and help them determine what broadband applications could help them meet their needs, regardless of the provider. FairPoint will help communities identify issues they are facing that can be addressed with broadband applications and will then work to provide those broadband services and applications. Tr. 9/20/07 at 187–188 (Nixon); tr. 9/21/07 at 10–12 (Nixon).

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246. Tr. 9/20/07 at 232 (Nixon).

247. Tr. 9/20/07 at 187 (Nixon); tr. 9/21/07 at 10–11 (Nixon).

453. As of September, 2007, FairPoint had already met with several economic development agencies. Tr. 9/20/07 at 187–189 (Nixon).

454. FairPoint does not anticipate that it would be the sole provider of broadband services or infrastructure. Once broadband needs are identified, FairPoint would work with other providers. In similar instances in the past, FairPoint collaborated with cable companies and several ILECs to develop a large fiber diversity ring around multiple counties. Tr. 9/21/07 at 11–12 (Nixon).

c. Discussion

FairPoint offers to support an economic development initiative that will, through a collaborative process, help advance local communities' application needs for the betterment of citizens and businesses. We appreciate the spirit in which FairPoint offers this economic development initiative. While this program could have significant value, the record does not disclose how large it is or how comprehensive will be the efforts under this program. Therefore, we conclude that it provides a benefit to the state, but we are unable to assess the degree of that benefit.

F. FairPoint's Transition Plans

1. General Findings

a. New Systems

455. Verizon's current "back-office" or business systems have been developed over many years to address Verizon's particular needs in serving customers in northern New England. Haga pf. at 4; Haga/Kurtze reb. pf. at 13–14.

456. FairPoint will replace Verizon's business systems with new systems. The business systems to be replaced include the computer software, hardware and interfaces that are the primary tools used to provide services and products to retail and wholesale customers. Haga pf. at 3–5; Nixon pf. at 23.

457. FairPoint decided to adopt new systems based on several factors. Most significantly, the new systems that will better provision existing services as well as potential new services. Second, many of the existing systems are proprietary and licensed to Verizon and the age and

functionality of the Verizon systems are limiting factors. For example, many of Verizon's systems utilize dated computer programming languages for which it is difficult to find support personnel. Finally, the Verizon systems were built over time for specific Verizon business functions that FairPoint does not intend to match. Haga pf. at 4–5; Haga/Kurtze reb. pf. at 13–15.

458. By deciding to use new systems, FairPoint may have more current information technology ("IT"), current languages running in distributed environments and the ability to take advantage of continuing technical advances. New systems also can be better integrated across applications, and they can reduce IT costs through combined functionality, which requires fewer transfers of data within the overall system architecture. Haga/Kurtze reb. pf. at 14–15.

459. Overall, the new system architecture will provide FairPoint an opportunity to offer new products, as well as existing products and services, in a way that is as efficient or more efficient than Verizon has offered in the past. Haga/Kurtze reb. pf. at 43.

460. Replacing the existing Verizon systems with "state-of-the art next generation applications" will be a positive development for all customers, once the systems are up and running. Tr. 9/19/07 at 164–165 (Mills); Mills pf. at 3.

461. In choosing new business systems to replace Verizon legacy systems, FairPoint and Capgemini have focused on functionality, vendor expertise and strength, the continuing support by vendors of the products and systems to be purchased, and price. Haga/Kurtze reb. pf. at 9.

462. FairPoint and Capgemini have evaluated existing implementations within the marketplace of the various products considered to date; FairPoint intends to install commercially-available systems in use today so that FairPoint may benefit from customer knowledge, as well as vendor experience and familiarity with systems. Haga/Kurtze reb. pf. at 9.

463. Verizon currently employs five major systems: CRIS, for residential customers; BCRIS, for business customers; Arbor, for broadband billing; CTIM, for centralized toll investigation mechanism; and NBBE, used to bill complex business accounts. Haga/Kurtze reb. pf. at 10.

464. FairPoint has selected replacement business systems for these systems and is moving forward with the testing of the new systems in the context of data-extract testing. Haga/Kurtze reb. pf. at 10–21; *see* tr. 9/18/07 at 164–165 (Haga), 190–191 (Haga, Kurtze).

b. Capgemini

465. FairPoint retained Capgemini to work with FairPoint to produce processes and operating methods that will utilize the new systems to successfully operate the Verizon wireline-based business. Nixon pf. at 17–18; Haga pf. at 5.

466. Capgemini plans to develop for FairPoint an entire suite of systems and operating infrastructure so that FairPoint can successfully assume control of (and operate) Verizon's Northern New England wireline-based businesses. The engagement requires the design of a systems architecture followed by a launching of that architecture, and finally, a migration of Verizon's data into the new FairPoint infrastructure. Capgemini is also designing and working with FairPoint to produce processes and operating methods that will utilize the new systems to successfully operate the Verizon wireline-based business. Haga/Kurtze reb. pf. at 4.

467. FairPoint began working with Capgemini in the fourth quarter of 2006 to develop the company's plan for the transition to the new FairPoint systems. Haga pf. at 5.

468. CapGemini intends to employ a team of up to 500 people on this project. Haga/Kurtze reb. pf. at 5.

469. Many Capgemini employees will be managed "off-shore." The large staff is intended to accelerate development and delivery. However, a team of this size and in multiple locations is difficult to manage effectively, and integration of numerous systems developed concurrently by separate large teams can be problematic. In addition, "off-shore" development personnel may not adequately understand the ILEC telecommunications business and operations, and this can produce problems in the software applications. Mills pf. at 17.

470. Capgemini has worked on similar projects and has experience in bringing together the implementation of a new suite of business systems, the business integration and the startup of data centers. The Capgemini team is expert in systems-application selection and development, data center operations and infrastructure construction and systems integration. Haga pf. 5–8; Haga/Kurtze reb. pf. at 6, 33–34; tr. 9/19/07 at 10–11, 16–17, 91 (Kurtze, Haga).

471. FairPoint's agreement with Capgemini provides for a flat fee to Capgemini so that FairPoint and Capgemini can focus on accuracy and, eventually, speed. FairPoint has not

pressured its Director of Billing and Operation Support Systems ("OSS"), who is responsible for managing the conversion, to trim costs associated with Capgemini. Tr. 9/19/07 at 19–20 (Haga).

c. Conversion Planning

472. "Conversion" or "cutover" is the process by which all data and business processes are transferred from the Verizon systems to their counterpart systems at FairPoint. The task involves a complex mapping of each source data element in Verizon's systems to the corresponding required data elements in FairPoint's systems, the development of conversion programs to automate the translation and loading of data to FairPoint's systems, and the confirmation that the FairPoint systems would operate accurately and responsively with the new data. Mills pf. at 5.

473. Conversion will require the replacement of most or all Verizon operational and business systems and the integration and conversion of over 1,500,000 new customers. Mills pf. at 5–6.

474. In planning for the cutover, FairPoint recognized the need for a continuing relationship with Verizon. Verizon and FairPoint executed the TSA to address the early stages of the transition until the new FairPoint systems are operational. The TSA will be in place at and after the closing in order to allow a properly-timed and prepared conversion. It sets forth the terms and conditions under which Verizon will continue to offer support services to FairPoint after the transaction closes, details the various services in terms of functionality, and provides for the structure of and timelines for a cutover planning process. Nixon pf. at 17–21; Haga pf. at 5; exh. PGN-1.

475. Under the TSA, FairPoint and Verizon have established a Joint Cutover Planning Committee that has two representatives from FairPoint and two from Verizon. FairPoint has allotted one of its two spots to a senior person from the Capgemini team. The committee is preparing a comprehensive conversion plan and have agreed to a transition with multiple phases and appropriate opportunities for thorough testing and evaluation at each stage. Haga/Kurtze reb. pf. at 22; Nixon pf. at 19.

476. Having Verizon provide certain support services beyond the closing date will allow FairPoint time to complete the design, testing and implementation of its new systems and to train

employees to work with the systems and thereby ensure an orderly conversion process. Nixon pf. at 20.

477. Two documents have been developed to manage the cutover. FairPoint and Capgemini have developed the FairPoint "Cutover Task List," which contains the planning and tasks to be completed by FairPoint during the conversion and thereafter. Verizon has developed the Verizon "Cutover Plan" that sets forth the tasks it must perform under the TSA and in connection with the conversion. The appropriate milestones are consistent in both plans. The two plans will be continually updated to provide greater detail. Haga/Kurtze reb. pf. at 22–27.

478. The cutover teams have been in constant communication to develop the revised documents. Both teams will continue the communication to develop more details within the respective plans and reduce risks associated with the cutover process. Haga/Kurtze reb. pf. at 27.

479. FairPoint intends to replace its existing computer applications while integrating the new business. These include most customer, inside and outside plant, provisioning, network related, and wholesale systems. The most difficult systems to replace are the Customer Relationship Management ("CRM") and Customer Billing Systems. Mills pf. at 5.

480. CRM systems include service order processing, sales, order management, billing adjustments, billing inquiry, and other functions. Commercially-available CRM software is largely unproven in high volume residential call centers. CRM systems involve a fundamental change in call center business processes, and they must be integrated with unrelated systems to share customer data, product data, plant inventory, and other information. The difficulty to implement new CRM systems in ILEC high volume residential call centers is evidenced by the fact that no large ILECs or Regional Bell Operating Companies have implemented new commercial CRM software systems for their high-volume regulated mass market businesses. Mills pf. at 9.

481. Customer Billing System implementation projects for ILECs are difficult since commercial software must be significantly customized before it can meet state-specific business requirements. Each state typically has unique regulatory or legacy functionality requirements. Mills pf. at 9.

482. FairPoint and Capgemini have organized the systems development work into four domains: Enterprise Resource Planning; CRM; OSS; and Information Systems. Haga pf. at 11.

483. Each of the domains and the systems they contain will be developed in four phases:

(a) identifying business requirements;

(b) designing, developing, and configuring the system;

(c) end-to-end testing; and

(d) training and migration.

Haga pf. at 11–12.

484. FairPoint has identified business requirements for both its retail and wholesale customers in each of the four domains. Haga pf. at 12–15.

485. Prior to the cutover, FairPoint plans to merge the conversion team with the permanent organization. Wheaton pf. at 25.

d. Design and Development

486. Over 500 people will be involved in the design and development phase of the project. Haga pf. at 17.

487. FairPoint is seeking to use Standard Application Program Interface-qualified programs so that the new systems can be better integrated. Haga pf. at 17.

488. After FairPoint has an understanding of the source data, it will develop programs that will read, format and insert the data into its applications. It will receive two test data extracts from Verizon. Haga pf. at 18.

489. FairPoint plans to have three "releases" or versions of its new software. The first will be available upon closing and will be used to perform tasks for FairPoint that are not otherwise provided by Verizon under the TSA. The second will include capabilities needed to perform the cutover. The third will include any deferred items and will include matters that may be useful later, such as marketing campaign management. Haga pf. at 21.

e. Testing

490. FairPoint and Capgemini have developed a comprehensive test strategy and plan. The cutover planning process has been extensively developed; additional detail is added as new information is obtained. Haga/Kurtze reb. pf. at 22–31; tr. 9/18/07 at 174–176 (Kurtze, Haga).

491. FairPoint will conduct systems testing in five phases:

(a) initial validation or unit test, which will ensure that the individual functions within an application work as intended in a stand-alone fashion;
(b) system test, which will use sample data to test the application functions within a system;
(c) functional/integration tests, which will indicate whether business processes that span multiple systems work as intended;
(d) performance testing, which will determine if the entire suite of systems supports the demands of the user community and the relevant business processes; and
(e) acceptance testing or operational readiness testing, which will involve FairPoint employees using the systems as customers would.

Haga pf. at 18–19; Haga/Kurtze reb. pf. at 31.

492. The test strategy plan will include the development of criteria that will create acceptance levels which must be met in order for cutover to proceed. FairPoint's testing process will test for its ability to comply with and measure all the metrics it must meet in Vermont; FairPoint and Capgemini are very confident that the systems will be able to capture all relevant data and to report that data as required in Vermont. FairPoint utilizes an application called Load Runner to simulate load volumes so that it can stress test its new system. FairPoint's testing plan will consume almost 200,000 man hours of testing. Testing and system remediation will continue under the comprehensive test strategy until the acceptance criteria are met. Tr. 9/18/07 at 180–181, 187–189 (Haga, Kurtze); tr. 9/19/07 at 77–79 (Haga); tr. 9/19/07 at 84 (Kurtze).

493. FairPoint's cutover readiness criteria include: the provision of training to wholesale customers; the provision of job aids and reference materials to wholesale customers; the development of escalation plans; the staffing and training of the retail and wholesale personnel; plans to address any wholesale customer data losses that might occur; having in place a license services administration group to handle pole and conduit license applications; and contingency planning. Tr. 9/18/07 at 147–149, 152, 165 (Haga).

494. In the event of a failure during cutover, FairPoint would operate the network manually and has begun to determine the staffing levels that would be required to do that. Tr. 9/18/07 at 162, 164–165 (Haga, Kurtze).

495. The E911 system is operated independently of the telephone company and is only modestly impacted by the transaction; FairPoint will test aspects of the system as necessary. Tr. 9/19/07 at 57–58 (Haga, Kurtz).

f. Wholesale Systems

496. The architecture of the new systems has been designed in a way to ensure parity between retail and wholesale customers. Tr. 9/18/07 at 195–196 (Haga, Kurtze); tr. 9/17/07 at 30 (Lippold); tr. 9/19/07 at 163–165 (Mills).

497. The fundamental business systems for retail and wholesale customers will be the same. The only difference will be how orders are entered into the systems. Tr. 9/18/07 at 195–196 (Haga, Kurtze).

498. Instead of the three systems presently used by Verizon for gateway access by wholesale customers, FairPoint will utilize a single gateway known as "Wisor" to interface with its wholesale customers. Wisor will provide access to wholesale customers through two means: web interface and "e-bonding." E-bonding means that the other carriers have or will have an electronic gateway for ordering. Haga/Kurtze reb. pf. at 15–16.

499. For wholesale customers who place orders via the web, to access the Wisor system the only change will be that they need to visit a new web site and enter a new URL. Tr. 9/18/07 at 149 (Haga).

500. FairPoint is discussing technical specifications with wholesale customers who use e-bonding. FairPoint will use industry standards for the interfaces and is not drastically changing the methods by which the companies communicate. To the extent that any wholesale customer has to make changes, FairPoint expects that the bonding interfaces will be in place six months before cutover so that the customer will have adequate time to make those changes. Tr. 9/18/07 at 150 (Haga, Kurtze); tr. 9/19/07 at 61–62 (Haga).

501. FairPoint will provide a web resource for its wholesale customers that is similar to what Verizon provides today. Tr. 9/18/07 at 151 (Haga).

502. FairPoint has provided a demonstration of the Wisor interface to wholesale customers and will provide training on Wisor access both via web interface and via e-bonding. Tr. 9/17/07 at 25–29, 35–36, 75 (Lippold).

503. The CLEC certification process is designed to test the system and not the processes. Tr. 9/18/07 at 186 (Haga).

504. CLECs will have 2-4 weeks to review and comment on FairPoint's testing plan. Tr. 9/18/07 at 179 (Haga, Kurtze).

505. FairPoint's cutover plans and certification process provide adequate opportunity for its wholesale customers to conduct testing and determine their ability to interface with the new system. Tr. 9/18/07 at 151 (Haga).

506. The testing and certification process for wholesale customers will include both the placement of orders and the flow through of the orders through FairPoint's back office system. Tr. 9/18/07 at 151–152 (Haga).

g. Training

507. FairPoint and Capgemini have begun work on the fourth phase of work, training and migration, and Capgemini is developing training plans for employees on the new systems. Tr. 9/19/07 at 53–55 (Haga, Kurtze).

h. Risks

508. The conversion process does not present risks to customers who have current service. They should see no change. Tr. 9/18/07 at 155 (Kurtze).

509. FairPoint has established a structure that shares risks with and creates incentives for Verizon and CapGemini, effectively creating a partnership with a vested interest in the timely success of the transition and conversion. The risk sharing limits the cost to FairPoint and provides incentives for each stakeholder to complete the projects expeditiously without endangering customer service to save money. Verizon shareholders' significant equity stake in

the new entity creates an incentive for the conversion to occur smoothly. Although Verizon would benefit from extended TSA payments, this could be at least partially offset by the increased equity value created in the new entity if the transition occurred quickly and without business disruption. Mills pf. at 12.

510. In general, the scope of FairPoint's project plan appears to be appropriately addressed. It includes business and systems integration and cut-over from Verizon to FairPoint systems and operations. The plan contains over 8,000 task items and is 175 pages long. Mills pf. at 14.

511. However, in spite of the size and length of the plan, many of the project areas will require additional detail to validate estimates and for execution. The existing plans lack detail necessary to confirm that task estimates are valid and provide adequate direction for actual work to be performed. A conversion work plan for a similar project would typically contain a significant amount of more detail. Other important tasks appear to be underestimated. Mills pf. at 15.

512. One of the critical success factors for any large business affecting system implementation is a dedicated executive sponsor with commitment to make the project successful. The level of commitment and investment that FairPoint has made in this area is exemplary. FairPoint has dedicated its President full-time to oversee the overall business integration project. In addition, key senior management personnel representing each area of the business have been assigned to the team full-time and report to the President. Mills pf. at 17–18.

513. CapGemini has dedicated a series of senior consultants to manage this project. They are experienced in large project management and experienced in the telecommunications industry. The full-time program manager is experienced in managing large complex projects. Although they are experienced in related areas, the assigned CapGemini senior management do not have personal experience implementing or converting ILEC customer systems for regulated mass market telephone service. This experience is an important determinant in successfully managing like projects. Mills pf. at 18.

514. It is common to find invalid or inaccurate legacy system data during conversion processes. Mills pf. at 11.

515. ILEC and customer conversion projects are difficult due to the wide variety of data involved, the disparate nature of the data on multiple source legacy systems, data integration requirements on target systems, differing data content and formats between the source and target systems, and often incorrect or incomplete source data. Mills pf. at 8.

516. Converting a large customer base to existing in-house systems is generally viewed as a high-risk effort in itself. Additional simultaneous systems projects are usually avoided to focus all attention on the conversion effort. There are many examples of project delays and customer service impacts from ILEC conversions when no legacy systems have been replaced at the same time. Mills pf. at 6.

517. It is difficult to coordinate simultaneous development with each project area changing during the process. Mills pf. at 10.

518. Replacement of ILEC operational and business systems, CRM and Customer Billing in particular, are also viewed as high risk projects. There are many examples of failed or delayed system replacement projects when no external conversions were involved. The combination of these efforts into simultaneous projects would increase the project risk above that of any single project. When a project is referred to as "high-risk," it does not imply that these potential issues are certainties. Rather, that there is a higher than normal possibility that problems could occur. This must be recognized, planned for, and managed accordingly. Mills pf. at 6.

519. FairPoint's conversion presents the following project risks:

- Customer service or accuracy problems negatively impacting retail customers;
- Service, performance, or accuracy problems negatively affecting wholesale customers;
- Project delivery schedules exceeded;
- Project cost budgets exceeded; or
- Compromises to system quality from rushing to meet deadlines or inadequate testing. System quality affects application stability which can affect customer service and accuracy.

Mills pf. at 6.

520. FairPoint recognizes that there are risks associated with the conversion process, including the risk of incomplete or inaccurate data mapping, poor performance or high fall-out

rates in the new systems and problems associated with the use of new systems by employees. Haga/Kurtze reb. pf. at 31; *see* exh. NECTA/Comcast-MDP-9R.

521. The most effective way to address conversion risks is through exhaustive planning, rigorous systems testing and employee training. Tr. 9/19/07 at 47–48 (Haga); Haga/Kurtze reb. pf. 31–32; tr. 9/19/07 at 54–55 (Haga, Kurtze).

522. A recent similar project at Hawaiian Telecom, where new systems were selected and implemented and the 600,000 access-line Hawaiian properties acquired from Verizon were converted, was considered unsuccessful. There were project delays and serious customer impacts after conversion. The Systems Integrator responsible for the system implementations and conversion is a large international firm with significant experience in the telecommunications industry. They recently settled a legal dispute with Hawaiian Telecom by paying them approximately $90,000,000. Mills pf. at 10.

523. The process followed by FairPoint, Capgemini and Verizon in Northern New England is significantly different than the process followed in Hawaii. The pre-conversion planning and preparation process is longer in northern New England than that provided for in Hawaii, giving the parties greater time to plan, test and prepare for the conversion. The majority of Hawaiian Telecom's problems, moreover, appear to have been flow-through related, and flow-through is a major portion of FairPoint's rigorous testing process and is not expected by FairPoint to be an issue during or after cutover. The original systems present in Hawaii were legacy GTE systems, and most of the systems present there are not present in Verizon's northern New England properties. In addition, FairPoint is an experienced telephone-systems operator, whereas the purchaser in Hawaii did not have comparable experience. Haga/Kurtze reb. pf. at 34–35; Smith reb. pf. at 11–12; tr. 9/18/07 at 162–163 (Kurtz).

i. Cutover Timing

524. Under the TSA, FairPoint must give a notice of readiness to cutover to Verizon sixty to ninety days prior to the actual cutover date and FairPoint will communicate that notice to all interested parties. Tr. 9/18/07 at 145, 194 (Haga).

525. During the cutover transition process, retail and wholesale customers will experience no effect on dial tone or daily telephone services, but they may experience some delay in the ordering of new services because such orders will need to be handled manually. Tr. 9/18/07 at 153, 155–156 (Haga, Kurtze), 160–161 (Haga).

526. FairPoint is planning for the cutover to occur on May 30, 2008, approximately four months after closing. From closing until the cutover date, FairPoint will be providing services to its customers using the legacy Verizon systems that are operating before closing. Haga/Kurtze reb. pf. at 28; tr. 9/19/07 at 34, 158 (Haga); tr. 9/19/07 at 51–53 (Kurtze).

527. Under the TSA, the final decision regarding whether to proceed with cutover rests with FairPoint. Tr. 9/18/07 at 145 (Haga); *see* tr. 9/7/07 at 42 (Smith).

528. Although FairPoint will decide when it is ready to cutover, based on the degree of cooperation between FairPoint and Verizon and based on the structure of the conversion management process, Verizon will be aware of FairPoint's progress and likely know prior to the notice of readiness that FairPoint is ready. Tr. 9/7/07 at 42 (Smith).

529. FairPoint plans to serve all customers under the TSA until it is satisfied that the new systems are ready to enable a smooth and seamless cutover for all services. Verizon has agreed to provide transition services to FairPoint for up to fifteen months after the closing. The TSA will continue, if necessary, after fifteen months with certain price adjustments. Haga pf. at 15, 23; Nixon pf. at 19, 20; Smith pf. at 23; Smith reb. pf. at 18; *see* exh. SES-4.

530. Having a successful cutover is much more important to FairPoint than cutting over on any particular date. Tr. 9/18/07 at 199–200 (Haga, Kurtze); tr. 9/19/07 at 36 (Haga).

531. Once the conversion begins, it must be completed. This will take approximately five days. The conversion cannot be broken into pieces that occur in separate off-peak intervals. Tr. 9/18/07 at 156–158 (Kurtze, Haga).

532. The conversion must occur at the end of a month to catch those files and data that require end-of-the-month processing from Verizon. No three-day weekends fall on the end of the month during 2008. Tr. 9/18/07 at 158 (Haga); tr. 9/19/07 at 42–43.

533. Because the cutover date will be known in advance by wholesale customers and others, advanced planning for the submission of orders should help alleviate service delays during the transition period. Tr. 9/19/07 at 155–156 (Haga, Kurtze).

534. FairPoint has requested interconnecting carriers to reduce the number of orders they would otherwise place during the two-week period prior to cutover in order to slow or reduce the number of moving pieces and somewhat ease the transition/cutover process. Tr. 9/18/07 at 154–155 (Haga, Kurtze).

535. During the five-day cutover period, parity between wholesale and retail customers will be ensured by the business processes that are in place, with parity determined using the same metrics. Tr. 9/18/07 at 159–160 (Haga, Kurtze).

536. Capgemini is developing the training for the newly-developed systems, and training is scheduled to take place following closing. Nixon reb. pf. at 27; Haga/Kurtze reb. pf. at 42.

2. Independent Monitor

a. Positions of the Parties

In condition number 14, the Department recommends that the Board direct FairPoint to engage an independent monitor selected by the Department for the system development and conversion process to ensure quality and readiness. The monitor's role would be to provide an unbiased view of project status and readiness for conversion with a focus on quality assurance. The monitor would interface directly with FairPoint and CapGemini project management and participate in status meetings for the overall project and the test activities for the key areas of the project. The monitor would define a group of key test criteria that would provide an objective measurement of conversion readiness.

- The test criteria would address the conversion process and system development completeness.
- The test criteria may include items that have been problems in the past.
- The test criteria would be communicated to FairPoint and CapGemini management in advance of testing so that they could incorporate the criteria into their mainline testing process for greater efficiency.

- The independent monitor would review the test plans in advance of test execution, participate in or observe testing, and review the detailed test results for each criteria.
- Upon completion, a report would be prepared and presented to the Board, the Department, and FairPoint management.

The monitor would also review overall test status and defect reporting at application and summary levels, review weekly and monthly project status reports for overall project status, and report monthly to the Department and FairPoint management.

FairPoint contends that an independent monitor for the systems development and conversion process is not necessary. FairPoint offers to make information available to the Department regarding the reporting of status, plan development and testing. FairPoint also notes that Capgemini is already providing an independent view of the conversion and that Capgemini itself has an independent review process and quality assurance team conducting regular and frequent project reviews to ensure quality and risk management.

Notwithstanding these observations, FairPoint offers to finance a consultant under slightly different terms. It proposes a single independent "joint expert" be engaged on behalf of the three northern New England states.[248] FairPoint argues that such a single expert would reduce confusion and delay, avoid the possibility of deadlock, and reduce cost.

Under FairPoint's plan, the goal would be to achieve an objective set of criteria that FairPoint and the expert agree will indicate readiness for cutover. When those criteria have been achieved, the decision to cut over would then be automatic. The expert would review FairPoint's testing and cutover readiness by reviewing FairPoint's testing strategy and testing plan, as well as FairPoint's test cases. The monitor would not have a role in review of system development because that process has progressed too far to offer meaningful review. Using well-defined testing criteria, the monitor would review and offer input regarding FairPoint's efforts to validate and confirm that the cutover will be successful and should proceed. The expert would be free to propose additional non-redundant tests and establish test defect severity level classifications. The expert would report to the Board and other Commissions and to the Department; the Board

248. FairPoint Brief at 145, et. seq.

and the Department also would have direct access to the expert. Any questions could be asked and answered, and all concerns fully addressed prior to FairPoint issuing the notice of readiness.

FairPoint provided more recent information in its Reply Brief, filed in early November. According to FairPoint, after the close of technical hearings in September, FairPoint worked with regulators in the three states to attempt to agree on the hiring of an Independent Monitor to represent the interests of all three states in reviewing the conversion process. These entities made substantial progress in defining a scope of work. Under the current proposal, state regulators would engage Liberty Consulting Group ("Liberty") as the Joint Independent Monitor. As before, funding would come from FairPoint. The scope of work would include:

- Review and assessment of FairPoint planned testing and cutover readiness process, including a review of staffing requirements and plans, training plans and schedules, business readiness and the concerns and requirements expressed by wholesale systems users;
- Monitoring of testing and cutover readiness process;
- Pre-cutover readiness review and final report;
- Post-cutover review and report; and
- State regulator reporting and oversight.

Liberty would generate key deliverables, including draft final reports for review by the Board and interested parties, and would participate in a status conference with the Board, prior to cutover, to present and answer questions from the Board on FairPoint's cutover readiness. Once a final agreement is reached, FairPoint offered to coordinate with the Department and ensure that the agreement is filed with the Board.

The Department objects to several aspects of FairPoint's plan, including that the scope of monitoring be limited.[249] The Department argues that FairPoint's proposal is "simply too narrow and fails to connect the monitoring to the bigger picture in a dynamic fashion."[250] The Department also prefers to have its own expert retained for this purpose.[251]

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249. DPS Reply Brief at 19.
250. DPS Reply Brief at 19.
251. DPS Reply Brief at 19.

b. Findings

537. Although FairPoint has executed a sound consulting contract with CapGemini, FairPoint does not have a seasoned expert who has either managed or monitored a systems development and conversion effort of this magnitude and whose prime responsibility is to oversee and manage this relationship. Wheaton pf. at 25.

538. Reporting to an independent monitor could inhibit the conversion process, delay progress and delay the transaction. Haga/Kurtze reb. pf. at 36.

539. FairPoint is willing to review its testing strategy, test plans and results with the Department. This would allow the Department to review information necessary to assess the various plans and the process would permit the process to continue and afford the Department an opportunity to make informed decisions. Haga/Kurtze reb. pf. at 32, 37.

c. Discussion

We agree that additional independent verification of the adequacy of FairPoint's conversion plans is needed. Not only is FairPoint converting data from many complex Verizon systems to its own databases, but those FairPoint systems are also new. Although Capgemini is heavily engaged in providing assistance and is itself experienced in these matters, no FairPoint employee has personal experience implementing or converting ILEC customer systems for regulated mass-market telephone service. Also, FairPoint Vermont's historical billing difficulties with prior conversons (discussed in Customer Service section, V.D.3) indicate a need for extra caution.

We also recognize that if we were to impose complex new procedural conditions on FairPoint in late December, the requirement would arrive after a great deal of complex work had already been done. FairPoint would need to work with the independent monitor to integrate his or her efforts into the existing processes so as not to jeopardize the timely completion of the work remaining. The risk of delays is greatly increased if each of the three states insists on appointing its own expert into a complex process that is already underway. Under the terms of the TSA with Verizon, delays increase costs for FairPoint, further exacerbating our concerns about its financial soundness.

The progress that FairPoint made after hearings, as reported in its Reply Brief, indicate that FairPoint is willing to provide a large portion of what the Department sought in condition number 14. In light of this progress, it is more reasonable to require FairPoint to work with the Department to develop a mutually acceptable proposal, subject to a few parameters that we set out here. First, we agree with FairPoint that a single monitor for the three states makes more sense than three separate monitors, provided that we can be assured that the Department's specific concerns will be fully evaluated. Second, the scope of work should include transition-related items discussed below on which we decline to adopt specific conditions, preferring to defer the issue to the Independent Monitor. Third, the monitor must have sufficient independence to be able to advise the Department and Board of the advisability of proceeding with cutover and other transition activities.

The Department and FairPoint should attempt to agree on an Independent Monitor and scope of work in advance of any further evidentiary hearings in this proceeding (assuming that FairPoint elects to submit the information necessary to address our financial concerns). If they are unable to reach an acceptable solution, we will resolve the issue expeditiously.

We commend FairPoint for offering to pay the costs of the independent monitor, but we are concerned that this will further financially weaken the company. To minimize the harm to FairPoint's financial soundness, we direct that the costs be divided between the two parties to the transaction, Verizon and FairPoint.

Accordingly, if we approved the merger, we would impose the following condition:

> **FairPoint shall hire an Independent Monitor acceptable to it and to the Department. The scope of work, which shall be developed jointly by the Department and FairPoint, would include:**
>
> - **Review and assessment of FairPoint planned testing and cutover readiness process, including a review of staffing requirements and plans, training plans and schedules, business readiness and the concerns and requirements expressed by wholesale systems users;**
> - **Monitoring of testing and cutover readiness process;**
> - **Pre-cutover readiness review and final report;**
> - **Post-cutover review and report; and**

- **State regulator reporting and oversight.**

The Independent Monitor will generate key deliverables, including draft final reports for review by the Board and interested parties, and will participate in a status conference with the Board, prior to cutover, to present and answer questions from the Board on FairPoint's cutover readiness.

Until FairPoint is obliged to give notice to Verizon to activate cutover on a specific date, the Board may order that cutover be delayed, if it has substantial concerns about FairPoint's readiness.

The cost of retaining Independent Monitor shall be divided equally between FairPoint and Verizon.

3. Pre-Cutover Audit

a. Positions of the Parties

In condition number 15, the Department recommends that the Board require FairPoint to conduct a conversion "audit" task to confirm conversion data accuracy for important data. This, the Department argues, would involve statistically valid sampling of important converted data within the new systems to ensure that it is accurate as designed and required for business operation. It would be executed on the final mock conversion in advance of cutover.

FairPoint maintains that the Independent Monitor would effectively address the concerns raised by the Department in Condition 15.[252]

b. Discussion

We agree with FairPoint that the establishment of the Independent Monitor makes it unnecessary to impose a separate condition of the kind proposed here. The Independent Monitor's ability to evaluate the adequacy and results of FairPoint's testing process achieves the underlying purpose. In addition, the Independent Monitor should have a broad enough scope of work to ensure that the purposes of the Department's proposed condition are met through FairPoint's testing.

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252. FairPoint Reply Brief at 11.

4. Switch-To-Bill-To-Tariff Review and Billing Audit

a. Positions of the Parties

In condition number 16, the Department recommends that the Board require FairPoint to evaluate the accuracy of billing information by performing a post-cutover "switch to bill to tariff" comparison. A sample of customers would be taken, served by multiple switches to determine the degree to which products that are provisioned on the switch are actually being billed to the customer, and that the products that are being billed to the customer meet the tariff requirements. The purpose of the comparison is to gain confidence that customers are being provisioned for the services on the switch for which they are being billed and that products for which they are being billed are correct as defined by the related tariff.[253] The review would confirm not only the accuracy of the conversion, but the accuracy of the current switch profiles, and the quality of the source billing data as it relates to the switches and tariffs. The review would be scheduled several months to six months after cutover, but could be conducted over a longer period.[254]

In condition number 17, the Department recommends that the Board should require a billing audit within six months of cutover. This would be a statistically valid sampling of representative billing output from multiple billing cycles. This review would include full invoice verification. It could be performed in conjunction with the "switch to bill to tariff" comparison and standard revenue operations production reviews.

FairPoint agrees to perform both of these operations, but over a longer time period. However, since the Department's witness did not consider the six-month time limit to be a hard-and-fast deadline, FairPoint commits to complete the requested audits within nine months of closing.[255]

b. Findings

540. A "switch-to-bill-to-tariff" comparison allows verification of the degree to which products that are provisioned on the switch are actually being billed to the customer, and that the products that are being billed to the customer meet the tariff requirements. Such reviews of

253. Mills sur. pf. at 10; tr. 9/19/07 at 186–187 (Mills).
254. Tr. 9/19/07 at 208–209 (Mills).
255. FairPoint PFD at 188–190; FairPoint Reply Brief at 12.

ILEC and Regional BOC data have been known to reveal billing discrepancies ranging from 8% to 27%. Mills sur. pf. at 7–8.

541. The odds of a successful conversion could be improved if FairPoint undertook measures such as: (1) a "switch-to-bill-to-tariff" comparison, which can help determine the accuracy of the switch profile set-up and converted billing records; (2) a billing audit conducted six months after cut-over; and (3) adding a conversion audit task to the conversion plans to confirm conversion data accuracy for important data. Mills sur. pf. at 10.

542. FairPoint does not yet have formal written policies and procedures that are critical for sound management of the transition and future operation of the New England Properties. Wierson pf. at 15–16.

543. A switch-to-bill-to-tariff comparison would be undertaken by FairPoint employees, taking them away from their normal duties and resulting in costs to the company. Tr. 9/19/07 at 208 (Mills).

544. The Department's proposed audit would include full invoice verification and would differ from the "switch-to-bill-to-tariff" audit in that it would look at all entries on a bill, including sales tax, surcharges and other entries that are not switch-driven. Mills sur. pf. at 10; tr. 9/19/07 at 192–193 (Mills).

545. FairPoint will undertake substantial testing prior to conversion to ensure that billing data is accurately transferred. Haga/Kurtze reb. pf. at 38; tr. 9/19/07 at 55–56 (Haga).

546. FairPoint will conduct total bill reviews as part of its normal operations and processes and will conduct audits as necessary when issues are discovered during the normal course of business. Haga/Kurtze reb. pf. at 38; tr. 9/19/07 at 39, 55–56 (Haga); tr. 9/20/07 at 157–158 (Nixon).

547. The Sarbanes-Oxley Act also places requirements on FairPoint to ensure the accuracy, validation and, if necessary remediation, of transferred customer information, and FairPoint is subject to audits under the Act. Tr. 9/19/07 at 39 (Haga).

548. FairPoint has committed to conduct a switch-to-bill-to-tariff audit within nine months of cutover, using a statistically significant sampling for both business and wholesale customers.

This will include items not included in tariffs or contracts, such as taxes or surcharges. *See* tr. 9/20/07 at 157–158 (Nixon).

c. Discussion

There is little disagreement here. FairPoint has offered to conduct a switch-to-bill-to-tariff comparison and a billing audit, both as requested by the Department. The disagreement concerns whether the work should be completed within six months or nine. The Department's witness did not express a strong preference for six, and we see no reason to conclude that nine is too long. We accept and rely upon FairPoint's offer of nine. Accordingly, if we approved the Proposed Transaction, we would adopt the following condition:

> **FairPoint shall conduct a post-cutover "switch to bill to tariff" comparison to determine the accuracy of the converted billing records. This review shall involve sampling the customer base represented on multiple representative switches to determine the degree to which products that are provisioned on the switch are actually being billed to the customer, and that the products that are being billed to the customer meet the tariff requirements. The review should examine not only the accuracy of the conversion, but also the accuracy of the current switch profiles, and the quality of the source billing data as it relates to the switches and tariffs. The review shall be completed no later than nine months after cutover and filed with the Board and parties to this docket.**

5. Automated Conversion Metrics

a. Positions of the Parties

In condition number 18, the Department recommends that the Board require that the Capgemini conversion team utilize automated comparative conversion metrics reporting of key count statistics between the Verizon systems and the converted data in the new systems. These would include access line counts by type, customer counts by type, product counts by product code, and similar information. The reporting would be used as a tool by the project team during the conversion testing to quickly identify data mapping and conversion process problems.

FairPoint's response to this request is cautious but cooperative. FairPoint suggests that engagement of the Independent Monitor would obviate the need for the requirement. However, "FairPoint nonetheless hereby commits to the requirements of Conditions 18 . . . to the extent [it is] not rendered moot."[256]

b. Discussion

This condition has been rendered moot by FairPoint's commitment to comply with the Department's proposed condition. In addition, our decision to require the Independent Monitor makes it unnecessary to incorporate the commitment as a condition; instead, the automated processes should be within the scope of the Independent Monitor's work . If the Capgemini team does not choose to use non-automated conversion metrics reporting, and if that causes uncertainty about the reliability of the conversion, the Independent Monitor will have the responsibility to take notice and report that fact to the Department and the Board.

6. Phased Cutover

a. Positions of the Parties

In condition number 19, the Department recommends that the Board should require that the actual cutover be executed in at least two phases, to simplify an initial conversion and cutover. The first phase would include the single state decided to be the most simple from a conversion perspective, and that state could be Vermont.[257] The second phase would include the remaining states and would occur two months after Phase 1 to allow for full monthly business cycle execution, issue discovery, and adequate time for remediation.[258]

FairPoint argues that it considered such a proposal and rejected it as creating unacceptable costs and risks. FairPoint argues that the Department has no direct knowledge of the incremental costs, which would be substantial, particularly when the decision is made so late in the conversion planning. Additionally, FairPoint contends that a phased cutover would create additional training and system needs, as well as increased opportunity for errors as the customer's

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256. FairPoint Reply Brief at 11.
257. Tr. 9/19/07 at 179–182 (Mills).
258. Mills sur. pf. at 11.

state would become a much more important variable. In its Reply Brief, FairPoint also reports that imposing this condition could "materially affect the likelihood of the transaction closing."[259]

Verizon argues against a state-by-state cutover, asserting that it would create an enormous amount of additional work and expense and would increase the level of complexity.[260]

b. Findings

549. FairPoint plans to convert all three states at the same time. Haga/Kurtze reb. pf. at 29; *see* tr. 9/18/07 at 156–158 (Haga, Kurtze).

550. A single conversion produces efficiencies and economies. However, it also increases the risk of surprise, and that could affect customers. There will be no way to "fall-back" to Verizon systems after the actual cutover. Since the new FairPoint systems will be in production for the first time after the cutover, all of the more than 1,500,000 access lines and related customers would be exposed to impact if there are unanticipated data, system, or business process problems. Mills pf. at 10; Mills sur. pf. at 3.

551. A phased, "one-state-first" cutover would expose a smaller and more easily managed group of customers to potential disruption than a flash cut. Following successful initial conversion of the first state, both remaining states could be converted together with much higher confidence. Mills sur. pf. at 4; tr. 9/19/07 at 173–180 (Mills).

552. A phased cutover would increase some risks and costs. It would increase delay, complexity and risks to customers in connection with the conversion. Current applications would have to be set up to recognize and split out that data by state. Haga/Kurtze reb. pf. at 29; Smith reb. pf. at 13–14; tr. 9/7/07 at 55 (Smith); tr. 9/19/07 at 31 (Kurtze).

553. During a phased cutover, FairPoint call centers that support all three states would be required to work with two applications for some period of time. This would create both training and operational issues, such as having to work with two sets of applications while entering orders or attempting to respond to immediate customer concerns. Haga/Kurtze reb. pf. at 29; tr. 9/19/07 at 30–31 (Haga).

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259. FairPoint Reply Brief at 32.

260. Verizon Reply Brief at 5.

554. Testing would become more complex with separate cutovers. In addition to systems-based testing, testing would need to include whether Verizon can extract data at a state level. Haga/Kurtze reb. pf. at 29–30; *see* Smith reb. pf. at 13–14.

c. Discussion

We agree with the Department that the risks of error are large and a one-state-first cutover could reduce some of those risks. It is true that, for the first state in a phased cutover, more human resources would be available per customer to address problems. However, if one state must go first, there is a good chance it will be Vermont, which has the smallest market. Of greater concern, a phased cutover adds new risks. The added complexity adds opportunities for new errors as additional data must be coded, and cutover must be done twice. In addition, a phased cutover increases the complexity of the work done by call center operators, creating additional opportunity for error. Thus the phased cutover offers only a slight advantage, and one that could well be offset by other, more serious problems. We decline to impose a condition recommended by the Department.

7. Updated Cutover Plan

a. Positions of the Parties

In prefiled testimony, the Department's witness Wierson noted that he had received a copy of Verizon's cutover plan in June of 2007, but that it was difficult to track the "Cutover Plan" from Verizon against the "Cutover Task List" from FairPoint.[261] He recommended that a single document be produced to ensure that they are properly correlated.[262] In its proposed condition number 20, the Department recommended that the Board require FairPoint and Verizon to:

> provide an updated Cutover Plan, Task Index, and other related documentation to the Board for review prior to the approval of the acquisition. It should include the integration of the newly acquired Network Element Managers during the TSA period and with the newly

261. Wierson sur. pf. at 6-7.

262. Wierson sur. pf. at 7.

> developed OSS. This updated Cutover Plan should be consistent, more equitable and agreed too [sic], at least in principal [sic], by Verizon and FairPoint. Some type of tracking system between the various documents should be incorporated if it is not already. If there are areas that are not defined or agreed too [sic] they should be identified as 'open items.' [263]

The Department argues that providing this information should not require any appreciable additional work for either FairPoint or Verizon.[264]

FairPoint's disagrees, arguing that the Department's underlying concerns are adequately addressed by appointment of the Independent Monitor and that the broad scope of the Independent Monitor's work renders the proposed condition moot.[265]

b. Discussion

We agree with FairPoint that the appointment of an independent monitor gives all parties adequate opportunities to evaluate whether Verizon's "Cutover Plan" and FairPoint's "Cutover Task List" are adequately integrated. The Independent Monitor's scope of work should include evaluating the companies' documentation. If there are issues that need to be addressed, the Monitor will bring them to the attention of the Department and Board. Accordingly, we decline to impose this condition.

8. Training Plan

a. Positions of the Parties

In condition number 22, the Department recommends that the Board require FairPoint to create a plan within 10-12 months after closing to transition and train Verizon employees, who are accustomed to Verizon's procedures, into FairPoint's operational processes. FairPoint should establish its own written policies and procedures and provide those along with the transition plan.

FairPoint agrees with the Department's proposed condition that the company should create a plan within ten to twelve months after closing to transition and train Verizon employees.

263. DPS Brief at 44.

264. DPS Brief at 44.

265. FairPoint Reply Brief at 11, n.3.

However, FairPoint notes that in order to have a successful conversion FairPoint will need to complete much of its training after closing and prior to cutover.[266]

b. Discussion

We accept FairPoint's commitment to create and file with the Department within ten to twelve months after closing to transition and train Verizon employees. If we approved the Proposed Transaction, we would adopt the following condition:

> **FairPoint shall create a plan within 10–12 months after closing to transition and train Verizon employees, who are accustomed to Verizon's procedures, into FairPoint's operational processes. FairPoint shall establish its own written policies and procedures. FairPoint shall file these policies and procedures along with the transition plan.**

9. Customer Guarantees for Errors

a. Positions of the Parties

In condition number 23, the Department recommends that FairPoint hold customers harmless from billing errors resulting from the conversion and not collect on any underbilling which may occur on consumer accounts as a result of the systems conversion.

In condition number 24, the Department recommends that the Board impose a condition requiring FairPoint to provide consumers with a billing accuracy guarantee. Under that guarantee, customers would receive a billing accuracy credit of $5.00 per month for every month the bill provided to the consumer from FairPoint contains an inaccuracy that is the result of a FairPoint error.

FairPoint opposes these conditions, arguing that such measures are unprecedented, that they amount to a penalty not justified by the record evidence, that they would be unmanageable to implement and potentially disruptive of customer relations, and that they would be a bad precedent for Vermont utilities that are considering whether to upgrade billing systems.[267]

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266. Nixon reb. pf. at 27; FairPoint Reply Brief at 11.
267. FairPoint Reply Brief at 38.

b. Findings

555. No hold-harmless condition or penalty similar to proposed condition number 23 has ever been imposed in the past. Tr. 9/21/07 at 141 (Pariseau).

556. While the hold-harmless proposed condition would not take effect until three months after conversion, it has no end date and would continue until FairPoint systems "no longer generated billing errors." Tr. 9/21/07 at 144–145 (Pariseau); tr. 9/20/07 at 244 (Nixon).

557. The Department's proposed condition numbers 23 and 24 would be difficult to administer, because they require a determination that a billing error resulted from the system conversion. Tr. 9/20/07 at 244–245 (Nixon).

558. FairPoint once issued a $5.00 credit to four customers for a billing error that involved three months worth of bills and that took longer than expected to resolve. Tr. 9/21/07 at 142 (Pariseau).

559. Proposed condition 24 would not take effect until three months after conversion. It has no end date and would continue each month until FairPoint systems "no longer generated billing errors." Tr. 9/21/07 at 144–145 (Pariseau); tr. 9/20/07 at 244 (Nixon).

c. Discussion

We agree with the Department that special conditions should be imposed to guarantee the accuracy of FairPoint's new billing systems. The risk of billing errors is so large that we need to adopt protection for consumers who may be adversely affected. To the extent that FairPoint's careful conversion, under the watchful eye of an Independent Monitor, reduces billing errors, penalty provisions such as those contemplated here would have no effect.

FairPoint observes that the Department's proposals have no termination date, and we agree that FairPoint should not be subjected indefinitely to such a penalty provision. We do not view the Department's proposals as an attempt to adopt permanent penalty mechanisms; instead, they are directed at protecting consumers from the potential for serious bill errors as a result of the transition of systems. To the extent that we would consider permanent mechanisms, we agree with FairPoint that it may be more appropriate to consider them in a generic proceeding or reopen the Incentive Regulation Plan. Nevertheless, we do think that a short-term penalty provision should be imposed as a guarantee and incentive for billing accuracy.[268]

FairPoint also observes, as to both proposals, that it would be difficult to determine which billing errors resulted from the conversion. We agree, and we omit that limitation here.

FairPoint also complains that under-billing to customers should not produce a penalty or a windfall to the customer. We agree that FairPoint should have the right to collect under-billed amounts from ratepayers. However, since the customer will be inconvenienced, the $5 credit should still apply.

Finally, FairPoint asserts that the proposed conditions could drive a wedge between FairPoint and its new customers and divert government and FairPoint resources from correcting any actual problems. While this is certainly possible, we think the reverse is more likely. Offering a customer a $5.00 credit because of an acknowledged company error has far more potential to create goodwill than the reverse. Moreover, our experience with electric utility service guarantees has not shown that they negatively affect customer relationships.

Therefore if we approved the merger, we would impose the following conditions:

> **During any of the first 18 monthly bills sent to customers under the new FairPoint billing systems, in each month in which the bill provided contains an error FairPoint shall provide each retail customer a credit of $5.00 (in addition to refunding any over-billing).**

G. Effect on competition

For years, the Board has established policies designed to open the Vermont telecommunications market to competition, with the expectation that competitive pressures will (over the long run) lead to a broader range of service choices and lower prices for consumers. Federal law (through the Act and FCC Orders) embodies the same concept. A significant component of these efforts has been the requirement that Verizon provide interconnection to competitors, including access to unbundled network elements at their long run incremental cost. Under Section 251 of the Act, all carriers must provide interconnection (unless exempted under

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268. We note that service guarantees are not new. Many of Vermont's electric utilities have included them in their Service Quality and Reliability Plans that we have approved over the years. The two largest electric utilities have guarantees of $10 and $25 for any billing error, quite higher than the modest amounts we adopt here.

Section 251(f)). To implement these requirements, Verizon now makes available a large number of UNEs. The Board, in Docket 5713, set the UNE prices.[269] In addition, Verizon has established its SGAT (required under Section 252(e) of the Act) which includes all of the UNEs that it makes available. Verizon has also negotiated a number of interconnection agreements (as provided under Section 252 of the Act). To supplement these arrangements, Verizon has entered into what it terms "commercial agreements" whereby it makes available certain UNEs that it is not required to provide under Section 251 of the Act.

CLECs have relied upon Verizon's UNEs and the obligation to interconnect to enter the market in Vermont. Any sale of Verizon's service territory has the potential to disrupt these arrangements. This could occur if FairPoint's interconnection obligations were not as extensive as Verizon's. It could also occur through the change of systems, including the OSS, whereby competitors obtain wholesale services from Verizon, including the cutover of systems.

To minimize these concerns FairPoint has made a series of commitments intended to maintain the status quo and allay any concerns about the effect of the Proposed Transaction on competition. These commitments are:

- FairPoint will assume all contracts and interconnection agreements governing service in the state of Vermont, and where that is not possible FairPoint will adopt contracts with substantially the same rates, terms and conditions.[270]
- FairPoint will agree to extend in writing all inter-carrier agreements (including interconnection agreements) in effect as of the closing date for three years following their stated expiration date.[271]
- In addition, for interconnection and other inter-carrier agreements with expired terms that are continued only on a month-to-month basis as of the closing, FairPoint will agree to extend the then-current rates and other terms in writing for three years following the transaction closing.[272]
- FairPoint will assume Verizon's rights and obligations under the terms of the Incentive Regulation Plan (including the applicability of the PAP for wholesale customers), and the SQ Plan, including the agreement under the Incentive Regulation Plan not to raise rates in tariffs for existing regulated intrastate

269. *Investigation into NET's tariff filing re: Open Network Architecture*, Docket 5713, Order of 2/4/00.

270. Skrivan reb. pf. at 6.

271. Skrivan reb. pf. at 6; FairPoint PFD.

272. Skrivan reb. pf. at 6; FairPoint PFD.

telecommunications services during the term of the Incentive Regulation Plan (through December 31, 2010).[273]

- FairPoint will agree that the newly certificated acquired operations will not assert rural exemptions under Section 251(f)(1) of the federal Communications Act. In addition, FairPoint has proposed that it will not seek any suspension or modification of any 251(b) or (c) obligation pursuant to Section 251(f)(2) of the Communications Act.[274]
- FairPoint will provide any item on the 14-point "competitive checklist" set forth in section 271(c)(2)(B) of the federal Communications Act that Verizon would be required to provide under the law, pursuant to the applicable pricing standard adopted by the FCC, even though FairPoint is not a Bell Operating Company (BOC) and will not be a BOC after closing.[275]
- FairPoint will implement systems that conform to industry standards.[276]
- FairPoint will agree not to recover transaction expenses from end users or wholesale service provider customers.[277] FairPoint expects to capitalize certain costs such as certain conversion and systems development costs that it reserves the right to seek recovery of in future rate cases.[278]
- FairPoint will install and test systems and provide CLECs an opportunity for training on such systems before cutover.[279]
- FairPoint will continue to offer all CLECs (and wholesale customer) services required to be offered by Verizon immediately prior to closing (including under wholesale tariffs, agreements, and the Statements of Generally Available Terms and Conditions ("SGAT")), including access to E911 systems, back-office support systems, directory listings, automated directory assistance, published network specification sheets, CLEC User forum information, and a CLEC handbook.[280]
- FairPoint will cap existing rates under wholesale tariffs in effect as of the closing at then-current levels for a period of three years following the transaction closing, and FairPoint will also freeze the wholesale discount offered under total service resale ("TSR") tariffs in effect as of the transaction closing date at then-current levels for three years after the transaction closing, unless FairPoint is required by

273. Skrivan reb. pf. at 7.
274. Skrivan reb. pf. at 7, 26-27; FairPoint PFD.
275. Nixon reb. pf. at 7; Lippold reb. pf. at 14–15.
276. Skrivan reb. pf. at 7.
277. Skrivan reb. pf. at 7.
278. Exh. FP Cross-3; tr. 9/7/07 at 186–192, 207–213 (Skrivan).
279. Skrivan reb. pf. at 7.
280. Skrivan reb. pf. at 7.

law to modify such rates (for example, due to a mandated revenue-neutral rate rebalancing).[281]

- FairPoint agrees that it will not withdraw any interstate or intrastate special access service or seek to increase any of its interstate or intrastate tariffed special access rates to be effective within three years after the transaction closing, unless required by law.[282]
- FairPoint will also assume SGAT in Vermont and agrees that the Vermont SGAT shall remain in place with rates capped at then-current levels for three years following the transaction closing.[283]
- FairPoint will prorate all volume pricing provided for in inter-carrier agreements, so such volume pricing terms will be deemed to exclude volume requirements from states outside of the three-state area following the closing. Verizon is contractually bound to do the same with respect to services it will continue providing in states outside the three-state area acquired by FairPoint.[284]

1. Positions of the Parties

FairPoint contends that the transaction poses no risk to competition in Vermont. According to FairPoint, its legal obligations, voluntary commitments, and improvements to OSS systems and interfaces will put wholesale customers in at least as good a position than they have been in with Verizon. FairPoint argues that competitors will have prices and other terms and conditions of service that are equal to or superior to Verizon's. Moreover, FairPoint maintains that its commitments (outlined above) will ensure that the competitive environment is not adversely affected. Finally, FairPoint states that its newly-developed wholesale systems will offer competitors higher-quality service than that to which they are accustomed.

The Department argues that the Board must adopt conditions to ensure that CLECs do not face actual or potential degradation of service as a result of the merger. These conditions include requiring FairPoint to meet the same obligations that Verizon now faces as a result of Sections 271 and 272 of the Act, barring FairPoint from seeking an exemption from interconnection obligations as a small or rural carrier under Section 251(f) of the Act, requiring FairPoint to

281. FairPoint PFD.

282. Skrivan reb. pf. at 7–8; FairPoint PFD.

283. Skrivan reb. pf. at 8.; FairPoint PFD.

284. Skrivan reb. pf. at 8.

continue and extend its duties under interconnection agreements and the SGAT, adopting the PAP, and establishing a rapid response team to address potential concerns arising from system conversions without the need for litigation.

The CLEC parties (NECTA/Comcast, Sovernet/segTEL, and One Communications) assert that the merger will result in obstructing or preventing competition in the wireline communications network. They argue that FairPoint has retreated on its commitment to be subject to the same regulatory obligations as Verizon, expressing concerns about the continued availability of UNEs, discrimination, wholesale service quality and support for the wholesale systems. In particular, they express concern about the OSS. In addition, they claim that FairPoint has failed to demonstrate sufficient financial resources and expertise to provide service equivalent to Verizon's.

2. The CLEC Settlement

On October 26, 2007, FairPoint filed the Stipulated Settlement Terms ("CLEC Settlement") among FairPoint and a number of CLECs that are parties to review of the transaction in the three northern New England states, including two CLECs that are parties to this proceeding — Sovernet and segTEL. Under the terms of the CLEC Settlement, the parties agreed to support approval of the transaction, subject to specific conditions set out in the agreement. The settling parties also agreed that if the conditions are not adopted in all material respects, and without material modification, by each state, they will be null and void in that state.[285] Notwithstanding this limitation, FairPoint states (referring to the CLEC Settlement conditions):

> Regardless of any settlement, however, the Board can and should adopt this particular articulation of FairPoint's commitments, in its entirety, as conditions of its approval of the transaction.[286]

To a large degree, the conditions agreed to in the CLEC Settlement overlap with the commitments made previously. Thus, the settlement addresses most CLEC concerns related to unbundling and includes provisions for maintaining and extending interconnection agreements

285. CLEC Settlement at 9.
286. FairPoint Reply Brief at 55.

and commercial agreements, adoption of the SGAT, making available UNEs (including some UNEs that the FCC no longer requires LECs to provide), and mandating that FairPoint continue to meet the same ordering intervals as has Verizon. The CLEC Settlement also incorporates similar commitments by FairPoint for the adoption of the PAP, maintaining special access rates. Finally, FairPoint has incorporated its commitments for education of CLECs concerning the new OSS systems; these are intended to help with the transition of systems from Verizon.

The Settlement also provides several enhancements:

- FairPoint will make available line sharing and wholesale DSL for a period of three years at a rate below FairPoint's retail rate.
- FairPoint will extend the terms of interconnection agreements for three years, rather than the one-year extension to which it previously agreed.
- FairPoint will not seek to have any of its wire centers to be "non-impaired" (which would allow it to withdraw the offering of certain UNEs.

One Communications and NECTA/Comcast each raised objections to portions of the CLEC Settlement. They argue that adoption of the CLEC Settlement may be discriminatory, as some of the agreement makes special arrangements only with respect to the settling parties. In addition, they assert that it does not go far enough on issues such as FairPoint's obligations under Sections 271 and 272 of the Act, PAP penalties, OSS, and compensation for CLEC costs arising from the need to convert systems to match the new FairPoint systems.

With two exceptions, if we were to approve the Proposed Transaction, we would adopt conditions that are not materially different from those set out in the CLEC Settlement. FairPoint's commitments go a long way towards addressing the concerns of CLECs in this proceeding. Moreover, our adoption of the Settlement terms will ensure that FairPoint's commitments apply to all CLECs, not just the signatories, thereby removing the risk that the Settlement may be discriminatory. The first condition we decline to adopt is the agreement that the PAP penalties for exceeding the wholesale service quality standards would not apply for the first month after the transition. We discuss this condition below as part of our discussion of the PAP. The second condition that we do not adopt from the CLEC Settlement's condition is a series of commitments related to the transition of systems and education of CLEC customers.

These are reasonable steps. However, the bulk of the dates agreed to by the stipulating parties have already passed, so the adoption would be largely moot.

3. Unbundling Obligations

a. Findings

560. To date, Vermont has experienced limited competition from CLECs. In the future, more competition is expected, in both the business and residential markets, from cable providers, cellular companies, and VoIP providers. Pelcovits pf. at 9–12; Docket 6959, Order of 9/26/05 at 90–103; Lippold reb. pf. at 16–17.

561. Following the transaction, FairPoint will be an ILEC that is subject to the interconnection obligations in sections 251 and 252 of the Act. These include the duty to provide access to UNEs and negotiate interconnection agreements in good faith. Skrivan reb. pf. at 24.

562. CLECs still depend on the incumbent LEC, in this case, Verizon, to provide interconnection (i.e., the ability to exchange traffic between a CLEC's customers and other customers), including UNEs, at reasonable rates, terms and conditions. Pelcovits pf. at 14–16.

563. The Board, Department, Verizon, and competitors have made significant investments of time, systems, plant and/or other resources to ensure a competitive marketplace can develop. Without the interconnection requirements that have been adopted, interconnection agreements, competitors would be unable to compete on anything near a level playing field with Verizon. Lafferty pf. at 14.

564. Subsequent to the closing of the Proposed Transaction, FairPoint will have the same market power in Vermont as Verizon. FairPoint will be the incumbent LEC in the same fashion as Verizon and use the same network with the same scale throughout the state as Verizon. It will operate the only network in Vermont which reaches all parts of the current Verizon territory and will maintain carrier of last resort obligations. Lafferty sur. pf. at 10.

565. A CLEC is entitled to obtain access to high capacity UNE loops or transport under section 251 if the CLEC would be "impaired" without access to such network element on an unbundled basis, or if the ILEC has agreed to provide such network element on a contractual

basis. There currently is no wire center in the state in which the ILEC would currently be relieved of its obligation to provide UNE loops under section 251(c). Skrivan reb. pf. at 25.

566. For transport (including DS-3) as well as for loops, all network elements required under section 251(c) continue to be provided in the state under regulated rates, terms, and conditions. Skrivan reb. pf. at 25.

567. FairPoint has committed to provide wholesale customers with the services of at least equal quality to what they receive from Verizon today. Lippold reb. pf. at 15, 20, 30.

568. FairPoint has committed to offer to CLECs those services that Verizon offers today in the state pursuant to tariff, interconnection agreements and the SGAT. Lippold reb. pf. at 14; Nixon reb. pf. at 8; Nixon pf. at 28; Leach pf. at 8; Skrivan reb. pf. at 4.

569. Following the closing, CLECs will receive all of the UNEs they receive from Verizon immediately prior to the closing, whether under a Section 251 interconnection agreement or under the SGAT. FairPoint also has committed to continue to provide additional services to CLECs under commercial agreements, including the same services that CLECs will be receiving immediately prior to the closing under commercial agreements with Verizon, such as the Wholesale Advantage agreements.[287] *See* Lippold reb. pf. at 14.

570. Rural telecommunications carriers are exempt from the interconnection and unbundling obligations in Section 251 of the Act; small carriers serving fewer than two percent of the access lines nationwide may also request to be exempt. 47 U.S.C. §251(f); Pelcovits pf. at 27.

571. FairPoint has committed not to seek an exemption from ILEC interconnection obligations within the Verizon footprint as a rural telephone company pursuant to Section 251(f)(1) of the Telecommunications Act. FairPoint also will not seek to divide the acquired Verizon territory into small companies that would individually qualify as rural telephone companies for purposes of seeking rural telephone company exemptions pursuant to 47 U.S.C. §251(f)(1). Nixon pf. 28, 33; exh. NECTA/CPVT-MDP-13; tr. 9/19/07 at 220 (Nixon); Skrivan reb. pf. at 26.

287. These agreements replaced Verizon's offering of the UNE-Platform or UNE-P service after the FCC allowed Verizon to discontinue the sale of UNE-P as an unbundled network element. The UNE-P service is functionally equivalent to resale of Verizon's service, although at lower rates than applies to direct resale.

572. Verizon in the aggregate has more than 2% of the nation's subscriber lines. As a result, Verizon is not a carrier entitled to seek suspensions or modifications of its Section 251 ILEC interconnection obligations pursuant to Section 251(f)(2) of the Telecommunications Act. Tr. 9/7/07 at 12 (Smith); Pelcovits reb. pf. at 6–7; Lafferty sur. pf. at 13.

573. If FairPoint were permitted to claim and seek a rural telephone company exemption from ILEC interconnection obligations competition could be adversely affected. Pelcovits pf. at 27–29; Lafferty reb. pf. at 13–14.

574. FairPoint has committed not to request a suspension or modification of interconnection obligations under Section 251(f)(2) of the Act. Nixon pf. at 28; Skrivan reb. pf. at 26.

575. FairPoint has committed to assume existing interconnection and other inter-carrier agreements with no diminution in services to CLECs, and CLECs will enjoy the same rate (including volume discounts) after the closing. FairPoint has committed to extend in writing all inter-carrier agreements in effect as of the closing date for three years following their stated expiration date. For interconnection and other inter-carrier agreements with expired terms that are continued or are only on a month-to-month basis as of the closing, FairPoint has committed to extend the then-current rates and other terms in writing for three years following the transaction closing. Nixon reb. pf. at 7; *see* Nixon pf. at 28.[288]

576. In the case of agreements that involve only one or more of the states of Vermont, New Hampshire, and Maine, FairPoint intends to assume those agreements completely, subject to consent where required. Nixon pf. at 28.

577. For existing interconnection agreements of Verizon New England that relate in part to service outside of those states, FairPoint has committed to offer the other party the same terms and conditions in Vermont, New Hampshire and/or Maine, mirroring the Verizon agreements wherever possible. Nixon pf. at 28.

578. The SGAT provides wholesale customers a single source of terms, rates and other information concerning all wholesale service an ILEC offers its competitors. Verizon has an approved SGAT in Vermont. Lafferty reb. pf. at 14.

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288. Mr. Nixon's testimony reflects this finding, except that his statements only incorporated a one-year extension. On Brief and in the CLEC Settlement, FairPoint extended its commitments to three years.

579. Bell Operating Committees ("BOCs") developed, filed and obtained approval of SGATs usually in conjunction with the review by state regulators of their petition to obtain Section 271 interLATA long distance authority. Verizon has an approved SGAT in Vermont. Lafferty sur. pf. at 14.

580. SGATs are similar to tariffs, although the approval process for changes can be different. Lafferty sur. pf. at 15.

581. FairPoint has committed to assume Verizon's SGAT. Skrivan reb. pf. at 8.

582. Verizon's SGAT is an important component of opening the Vermont local exchange market to competition. Lafferty sur. pf. at 14–15.

583. FairPoint has agreed to assume or replicate Verizon's interconnection and traffic exchange agreements, as well as to honor Verizon's interconnection agreements and to comply with the obligations of Section 251 of the 1996 Act. Skrivan reb. pf. at 6.

584. FairPoint and individual CLECs or groups of competitors can negotiate different requirements as part of an interconnection agreement. Thus, FairPoint (and competitors) do not lose any flexibility to customize solutions to individual circumstances. Lafferty sur. pf. at 16.

585. FairPoint has committed to cap rates on wholesale tariffs and the Vermont SGAT for three years following the transaction closing. Skrivan reb. pf. at 8.[289]

b. Discussion

The area of greatest concern to CLECs is the continued availability of the UNEs on which they rely. Under state and federal law, Verizon has an obligation to make available UNEs whenever a competitor would be impaired without access to a particular UNE. In Docket 5713, the Board evaluated the scope of this obligation and delineated the UNEs that Verizon had an obligation to provide.[290] The Board expanded the UNEs in Docket 5900.[291] In addition, the

289. FairPoint's agreement to the specific commitments reflected here are included in its Brief.

290. Docket 5713, Orders of 5/29/96 and 2/4/00.

291. *In re Joint Petition of New England Telephone & Telegraph Co. d/b/a NYNEX*, Docket 5900, Order of 6/2/99.

Board has established the pricing methodology that applies to both UNEs and the resale of services and has specifically set the appropriate rates.[292]

In accordance with the requirements of Section 252 of the Act, Verizon has entered into numerous interconnection agreements with individual CLECs in which the parties to the agreement have agreed to specific terms and conditions, including pricing. In addition, Verizon has established the SGAT. This document, which is similar to a tariff, sets out the UNEs that Verizon will provide, including the prices and other terms and conditions that apply.[293]

As outlined above, FairPoint has made a number of commitments that would essentially provide CLECs with the same UNEs, prices, and interconnection arrangements that they receive from Verizon today. FairPoint plans to adopt the existing interconnection agreements and the SGAT. In addition, to provide stability to CLECs, FairPoint has agreed to extend the existing agreements by three years. This extension would also apply to now-expired interconnection agreements. FairPoint also will continue in effect the commercial agreements under which Verizon now offers certain UNEs that it is not obligated to provide under Section 251. FairPoint has also now stated, unequivocally, that it will not seek to exempt itself from interconnection obligations under Section 251(f).[294] And FairPoint has agreed that, for three years, it will not seek to reduce these unbundling obligations by requesting the FCC to delist UNEs.

Our Order reflects the conditions sought by the Department, FairPoint's commitments, as well as those advocated in the CLEC Settlement.[295] In terms of interconnection obligations, there is no conflict between these proposals. These conditions should ensure that interconnection arrangements are equivalent to those available today. More broadly, we accept the Department's recommendation that we impose a condition requiring FairPoint to adopt all other Section 251 and 252 obligations of Verizon. This would encompass certain interconnection practices that are

292. Docket 5713, Order of 2/4/00.

293. 47 U.S.C. § 252(f).

294. Section 251(f) has two subparts under which certain ILECs may be exempt from interconnection requirements. Under subsection (f)(1), small carriers are exempt unless the Board affirmatively decides to extend the interconnection obligations. FairPoint agrees that it is now too large to qualify for the exemption.

Under subsection (f)(2), carriers with fewer than 2 percent of the access lines nationwide (which would include FairPoint) may request the Board to exempt them from unbundling obligations. FairPoint has agreed not to seek such an exemption.

295. Because these conditions are extensive, they are included only in the Order and are not reiterated in the text.

not necessarily embedded in the interconnection agreement and the SGAT. For example, FairPoint would be expected to adhere to the same trunk ordering intervals that Verizon now meets. Also included would be Verizon's policies related to number porting, tandem transit service, and mid-span meet arrangements.[296]

4. Section 271 and 272 Obligations

a. Findings

586. Verizon is a BOC and operates within Vermont as an ILEC. As a BOC, Verizon has certain additional responsibilities under the Act and FCC Orders. These arise primarily under Sections 271 and 272 of the Act. By contrast, FairPoint is not a BOC. Pelcovits pf. at 27; tr. 9/7/07 at 11 (Smith); 47 U.S.C. §271; Lafferty sur. pf. at 8–9.

587. Absent the requirements of Section 271, FairPoint's obligations to provide certain UNEs will be limited to those available under the FCC's impairment analysis. The FCC has ruled that, even if a UNE is no longer required based upon the 251 necessary and impair standard, it still may be required under Section 271. Ball pf. at 18; Lafferty sur. pf. at 11.

588. FairPoint has committed to provide anything that Verizon would be required to provide under the 14-point competitive "checklist" set forth in section 271(c)(2)(B) of the Act, pursuant to the applicable pricing standard adopted by the FCC. Skrivan reb. pf. at 28; Nixon reb. pf. at 7; Lippold reb. pf. at 14; Skrivan reb. pf. at 29.

589. FairPoint also has committed to honor Verizon's commercial contracts including those for items not required under the Section 271(c)(2)(B) checklist. Skrivan reb. pf. at 29.

590. FairPoint has also committed that, to the extent that Verizon is providing other services (such as line sharing and certain dark fiber facilities), FairPoint will continue providing them pursuant to agreements in place at the time of closing. Nixon reb. pf. at 8.

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296. This condition should address NECTA/Comcast's concern that FairPoint may not provide the same level of CLEC services that Verizon now does with respect to practices not explicitly delineated in interconnection agreements or the SGAT.

b. Discussion

Verizon's obligations to its competitors do not arise solely from Section 251 of the Act. At the time that the 1996 Act was enacted, BOCs, such as Verizon, were prohibited from offering interstate long-distance service originating in their service territories. In Section 271, the Act provided a mechanism by which BOCs could obtain authorization to enter the long-distance market if they could demonstrate that the local exchange market in the state was open to competition. This availability of competition was evaluated using 14 criteria set out in Section 271, which has generally been referred to as the competitive checklist.

In 2002, Verizon sought and received permission from the FCC to enter the long-distance market in Vermont. As part of that process, the Board conducted a detailed evaluation of Verizon's compliance with the checklist, which was forwarded to the FCC.[297] Compliance with the competitive checklist and Section 271 requirements has helped to open the market to competition in Vermont.

The reliance on Section 271 has become more important in the aftermath of FCC decisions that have limited the scope of the interconnection and unbundling obligations under Section 251. In particular, the FCC has determined that certain UNEs no longer have to be provided under Section 251 because competitors would not be impaired without access to those elements from the ILEC. The Board has reflected the federal decision, finding that network facilities and services that have been de-listed as UNEs by the FCC are not required to be offered in the state as UNEs, with rates based upon long-run incremental cost.[298]

FairPoint is not a BOC; as a result, under federal law, it is not required to comply with Section 271. As a result, the potential exists for the scope of competition in Vermont to be reduced as a result of the Proposed Transaction as the scope of FairPoint's obligations may be less than those of Verizon. To rectify this, several parties have suggested that we explicitly require that FairPoint be subject to Section 271 as if it were a BOC. One Communications goes

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297. *Petition of Verizon New England Inc., d/b/a Verizon Vermont, for Arbitration of an Amendment to Interconnection Agreements*, Docket 6533, Order of 2/6/02.

298. *In Re: Petition of Verizon New England, Inc., d/b/a Verizon Vermont, for Arbitration of an Amendment to Interconnected Agreements with Competitive Local Exchange Carriers*, Docket 6932, Order of 2/27/06.

beyond this and requests explicitly that we treat FairPoint as a BOC to ensure that both Section 271 and the nondiscrimination requirements of Section 272 of the Act apply.

FairPoint has largely addressed the concerns of other parties. Notwithstanding the fact that it is not a BOC, FairPoint has agreed to provide anything that Verizon would be required to provide under section 271(c)(2)(B) of the federal Communications Act, pursuant to the applicable pricing standard adopted by the FCC.[299] Through the CLEC Settlement, FairPoint will negotiate in good faith when a CLEC asks for an element. Moreover, to the extent that Maine or New Hampshire adopt additional Section 271 elements, FairPoint will provide them here.[300] To ensure that all CLECs have access to these elements, we will adopt the conditions related to Section 271 recommended by the Department and advocated as part of the CLEC Settlement.

We are unpersuaded of the need to formally state that FairPoint will be treated as a BOC as advocated by One Communications. FairPoint's commitments, coupled with our incorporation of conditions that reflect these conditions, will achieve the result that One Communications seeks — the availability of UNEs under Section 271 at just and reasonable rates.

The one other area of disagreement among the parties is the applicability of Section 272 of the Act. That section sets out safeguards for BOCs intended to protect their competitors. These include the requirement of a separate subsidiary for interstate long-distance service (although that mandate has lapsed) and, in Section 272(e), affiliate transaction requirements. These would essentially require FairPoint to make available to its competitors any services it provides its LEC affiliates on the same terms and conditions and at similar intervals. FairPoint contends that it is not subject to Section 272. In addition, FairPoint argues that the FCC's detailed cost accounting rules would adequately protect consumers.

By its own terms, Section 272 is not applicable to FairPoint. However, the affiliate transaction requirements that it incorporates reflect sound policy and are consistent with

299. Lippold reb. pf. at 15.

300. Both New Hampshire and Maine previously identified additional unbundling obligation under Section 271. The U.S. Court of Appeals for the First Circuit held in September that the states could not adopt these requirements. *Verizon New England, Inc. Vs. Maine P.U.C.*, Case Nos. 06-2151, -6-2429 (slip op. Sept. 6, 2007). That decision has been appealed to the U. S. Supreme Court.

standards that this Board has previously enunciated. For example, we have made clear that Verizon is subject to an imputation standard, equivalent to that set out in subsection 272(e)(3).[301] Therefore, we agree with the Department that we should, as a matter of state law, adopt the same standard for FairPoint. If we approved the Proposed Transaction, we would adopt the following condition:

FairPoint shall comply with the requirements of Section 272(e) of the Act.

5. PAP

a. Findings

591. Verizon has specific wholesale service quality obligations in Vermont. These are incorporated into the PAP, which the Board accepted as a condition of a favorable recommendation to the FCC on Verizon's application under Section 271 of the Act. Lafferty pf. at 32; Docket 6533, Order of 2/6/02.

592. FairPoint has committed to abide by the PAP in Vermont. FairPoint also will consider unifying and simplifying the PAP going forward. Lippold reb. pf. at 15; Skrivan reb. pf. at 7.

593. It is critical for CLECs that the PAP apply during the period around the cut over of systems from Verizon to FairPoint. Tr. 9/7/07 at 181 (Skrivan).

b. Discussion

As part of its petition to the FCC for authorization under Section 271 and request to the Board for a favorable recommendation on that petition, Verizon proposed the PAP. The Board accepted the proposal and adopted the PAP. The PAP establishes specific compensation that must be paid to CLECs in the event that Verizon does not adhere to specified service quality standards. The standards in the PAP are based upon the Carrier-to-Carrier standards ("C2C") that the Board originally adopted in Dockets 6167/6189.[302] At the present time, the PAP and the

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301. *Investigation into three special contracts filed by New England Telephone*, Docket 6077, Order of 2/8/00.

302. Dockets 6167/6189, Order of 3/24/00 at 147–150.

C2C standards are linked to similar wholesale performance measures and performance plan in New York, particularly in terms of the standards that are monitored.[303]

Several parties recommend that we specifically adopt the PAP in Vermont. The Department, in Conditions 28 and 29, asks that we adopt the existing PAP and freeze it in place until the Board adopts a successor PAP. FairPoint has agreed with these conditions.[304] In addition, as part of the CLEC Settlement, FairPoint specifically agreed to adopt the existing C2C standards.

One Communications and Sovernet also expressed concern over testimony by a FairPoint witness that it would seek a "grace period" extending from one-month prior to cutover until three months after cutover, during which the PAP would not apply.[305] Finally, several parties raised questions about whether FairPoint would accept the Board's jurisdiction over the PAP (since it arose from Verizon's status as a BOC). FairPoint has agreed that it will not challenge the Board's jurisdiction in this area. This is included as a specific condition of the CLEC Settlement.

We agree that it is appropriate to require FairPoint to adopt the PAP in Vermont. Accordingly, we would adopt the following condition if we approved the Proposed Transaction:

> **FairPoint shall adopt and be subject to the Performance Assurance Plan ("PAP") and the Carrier-to-Carrier standards that now apply to Verizon in Vermont. The terms and conditions of the PAP shall remain in effect and applied to FairPoint until the Board orders a successor PAP**

We also find no basis for granting a grace period during the transition from Verizon's systems to FairPoint's. In fact, this is precisely the period when CLECs have the potential to be most significantly affected; it would make little sense to take away the protection of the PAP during this period. To do so would shift the risk of wholesale service quality problems during the transition from FairPoint (which is the cause of the transition) to the wholesale customers who have no choice in the matter and generally no alternative means of obtaining service. Such a risk shift is unfair.

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303. Campbell pf. at 33.

304. FairPoint Reply Brief, Attachment 1 at 6 and Attachment 2 at 4, 8.

305. Tr. 7/7/07 at 180–183 (Skrivan). They argue that such a period is inappropriate.

6. FairPoint's Wholesale Services and Operation Support Systems

a. Findings

594. FairPoint will not be obtaining Verizon's wholesale organization, including the OSS. Instead, FairPoint will build its own organization and systems and will use the TSA for a limited time. Ball pf. at 8; Haga pf. at 4–5, 10; Lippold reb. pf. at 3.

595. Capgemini is developing the back-office systems required for FairPoint's wholesale operations. Lippold reb. pf. at 3.

596. The new systems and processes will be similar to Verizon's existing systems and will use the same industry standards that Verizon now uses. These include the ordering, billing, and trouble management systems. Lippold reb. pf. at 3–6.

597. FairPoint plans to employ the same electronic interface standards by order type that Verizon supports today. FairPoint also intends to use the industry-standard Order and Billing Forum versions and processes, even where Verizon has not in the past. Lippold supp. pf. at 1; Haga/Kurtze reb. pf. at 41; Lippold reb. pf. at 3–4; Haga pf. at 14–15.

598. FairPoint intends to use a vendor for both access and wholesale billing; the vendor will adhere to common bill standards and will support the creation of electronic bills or a paper format. Lippold supp. pf. at 1–2; Lippold reb. pf. at 5.

599. FairPoint will not offer its wholesale customers the same alternatives for billing as Verizon. FairPoint will only support paper statements and on-line statements. Lafferty sur. pf. at 26.

600. In instances where there will be some changes, those changes are as a result of new or updated industry standards that are intended to be uniform across the nation. Lippold reb. pf. at 6.

601. FairPoint intends to maintain parity between retail and wholesale orders; all wholesale orders will be treated with the same dispatch and will be placed into the same provisioning system as are retail orders. After wholesale orders are entered through FairPoint's OSS system, the order flows through the same processing systems as do retail orders. Lippold reb. pf. at 4; tr. 9/7/07 at 275 (Lippold); tr. 9/17/07 at 30 (Lippold).

602. Parity between wholesale and retail customers during the TSA period will be ensured in the same manner as it is today in Verizon's systems. Tr. 9/17/07 at 71 (Lippold).

603. By using industry-standard systems, FairPoint's OSS should provide wholesale customers at least the same level of service as do Verizon's systems. Lafferty sur. pf. at 24; Lippold reb. pf. at 3–6, 21–22; tr. 9/7/07 at 74 (Lippold).

604. FairPoint has committed to work with CLECs to test the new FairPoint systems prior to cutover, and ensure that the CLECs can use the new systems. Tr. 9/17/07 at 78 (Lippold); Haga/Kurtze reb. pf. at 40; Lippold reb. pf. at 7.

605. Neighboring carriers are at risk for incurring expenses to adapt to OSS changes FairPoint makes to implement the Proposed Transaction. Some of these neighboring carriers are relatively small companies. Lafferty sur. pf. at 26.

606. When Verizon introduces new systems or makes changes to existing systems,Verizon usually leaves the old system in place to provide CLECs time to adopt the changes. Lafferty sur. pf. at 25.

607. FairPoint's wholesale division will have account teams, a sales engineering team, and a contract management team. Lippold reb. pf. at 9–10; Lippold supp. pf. at 2–3.

608. In total, the wholesale operation will employ approximately 75-100 people, all of whom have relevant wholesale or telecom experience. Lippold reb. pf. at 10.

609. FairPoint's training program for its business and wholesale organization will cover a full range of issues relating to the services it provides. Lippold reb. pf. at 11–12.

610. The provisioning of services for wholesale customers will be performed by employees within the three-state region. This will use the wholesale provisioning team that Verizon now uses (and which will transfer to FairPoint), which today provides services to not only the three-state region, but also to states outside the region. Harrington/Brown/Smee reb. pf. at 21.

611. A dedicated outside plant technician work force for wholesale orders and troubles also will move to FairPoint. Harrington/Brown/Smee reb. pf. at 21.

612. FairPoint expects to have sufficient field technical forces to continue provisioning (and repairing) services as are provided today by Verizon. Harrington/Brown/Smee reb. pf. at 21.

613. FairPoint will also add a local number portability administrator prior to closing. Harrington/Brown/Smee reb. pf. at 21.

614. Between the Verizon employees that will transfer to FairPoint and the individuals that FairPoint will hire, FairPoint's wholesale operations will be fully staffed at closing. Tr. 9/7/07 at 247-248 (Lippold); tr. 9/17/07 at 21 (Lippold).

615. FairPoint intends to continue the CLEC User Group Forum currently sponsored by Verizon, which will provide a more formal process by which wholesale customers may provide input. Lippold reb. pf. at 8.

616. FairPoint will prevent the misuse of wholesale customers' business information in two respects: first, FairPoint will establish a code of conduct for its wholesale and business division personnel; and second, FairPoint's systems will have controls in place—for instance, to prevent employees from accessing carrier or customers' proprietary information in violation of Section 222 of the Communications Act—to prevent the opportunity for employees to misuse such information. Tr. 9/17/07 at 67–68, 97–100 (Lippold).

617. In the event of problems, wholesale customers will have a customer-specific account team comprised of FairPoint representatives with whom they deal on a regular basis; the customer will also have an escalation list and the home telephone number of the head of wholesale operations so that problems can be promptly resolved. Tr. 9/7/07 at 278 (Lippold).

b. Discussion

As a result of the merger, FairPoint will take over Verizon's wholesale operation, including the OSS system that CLECs rely upon for ordering, provisioning and maintenance of UNEs. FairPoint intends to provide the same level of service as Verizon does now. It will use industry standard interfaces, which provide CLECs with options as to how they want to interact with FairPoint's system. But the OSS that FairPoint will use is new; Verizon's wholesale operations systems will remain with Verizon and FairPoint must establish its own. Like other elements of the transition, some risks occur that the transition from Verizon to FairPoint will not go smoothly. We expect that the use of the Independent Monitor (as described above) will help address these concerns.

In the context of the OSS system, the Department and NECTA/Comcast raise the concern that, even if the transition goes smoothly, FairPoint's establishment of an entirely new operation with different systems may cause CLECs to incur additional costs to adapt their own interfaces to FairPoint's.[306] In addition, NECTA/Comcast asks that the Board require FairPoint to reimburse wholesale customers for incremental costs it may incur during the transition to initiate manual rather than electronic ordering processes. Finally, NECTA/Comcast request that the Board establish a fund to secure wholesale customers against direct damages in the event of a major cutover failure. FairPoint opposes these recommendations, characterizing compensation as unprecented, particularly since its new systems will comply with current industry standards.[307]

We reach the same conclusion here that we did for incremental costs that interconnecting companies may need to incur as a result of the conversion to FairPoint. In general, FairPoint should bear no obligation to pay CLEC costs arising from the need to adapt to the new systems. Verizon is free today to modify its OSS; the Board has not required, and no CLEC has requested, that the Verizon compensate the CLEC for costs it may need to incur as a result. As FairPoint argues, imposing such costs could create a disincentive to improve systems. However, because of the possibility that individual CLECs may need to make more significant adjustments, if an interconnecting system or CLEC faces costs that are both extraordinary and not consistent with the types of costs to interconnecting carriers arising from the ordinary course of business, a carrier may petition the Board to require FairPoint to compensate them for the atypical expenditures.

NECTA/Comcast also raise a concern with the provisions of the CLEC Settlement that establish a process for coordination of transition activities, including training. NECTA/Comcast maintain that the Settlement has unrealistic timelines, insufficient provisions related to cutover readiness, and no provision allowing the Board to preempt a premature cutover. These issues are addressed above as part of our consideration of the transition and cutover of systems, through requiring FairPoint to hire an Independent Monitor. In addition, the CLEC Settlement sets out an educational plan that should help CLECs manage the transition.

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306. Lafferty pf. at 30; Lafferty sur. pf. at 26.

307. Lippold reb. pf. at 19–20.

7. Rapid Response Team

a. Findings

618. A "rapid response" team is designed to provide a mechanism to attempt to address interconnection disputes arising out of the transition quickly and without resorting to litigation. Tr. 9/21/07 at 196 (Campbell); Lafferty sur. pf. at 30; Ball pf. at 12.

619. The challenges faced by FairPoint becoming the largest ILEC in several states, including the creation of an entirely new OSS platform, raise the potential for more disputes than normal. The rapid response team would be a vehicle to quickly respond to problems which could not have been foreseen. Lafferty sur. pf. at 30.

b. Discussion

Sovernet/segTEL and the Department (in Condition 34) recommend that the Board require FairPoint to work with CLECs to jointly develop a rapid response team. This team would be intended to respond quickly to unforseen issues affecting CLECs that may arise from the transition to FairPoint's newly developed systems. The Department proposes that FairPoint submit the proposal within six months of closing.[308]

FairPoint states that a rapid response team is unnecessary. However, FairPoint has agreed to this condition.[309]

We accept the parties' agreement to the development of a rapid response team to address CLEC transition issues. We expect that, notwithstanding FairPoint's best efforts to manage the transition from Verizon, some issues will arise. Most of these are likely to be resolvable between FairPoint and the affected customer(s). It is possible, however, that some will require a level of dispute resolution. The rapid response team may help in this process. In addition, if necessary, the Board can respond quickly to disputes that may arise, either formally (through a docket) or through informal means if the parties request it.

If we approved the Proposed Transaction, we would adopt the following condition.

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308. Lafferty sur. pf. at 30; exh. DPS-CLC-5.
309. FairPoint Reply Brief at 15.

No later than six months after closing, FairPoint shall, after consultation with its wholesale customers file a proposal to the Board for a "Rapid Response Team" to address issues with wholesale customers arising from the transition from Verizon to FairPoint.

8. Interconnection Services Tariffs and Special Access Prices

a. Findings

620. Verizon offers Special Access volume and term plans to its access customers. Customers can pay a lower price by purchasing a larger number of circuits or services and committing to a longer term. Lafferty pf. at 17.

621. Intrastate Special Access prices are capped under Verizon's Incentive Regulation Plan in Vermont. In addition, the majority of Special Access services are purchased through an interstate access tariff. Lafferty pf. at 17.

622. The transfer of ownership to Verizon may reduce the total volume of access services purchased by another carrier (or even an end-user customer) from FairPoint or Verizon, resulting in an increased price for the same services purchased from Verizon before the transaction. Lafferty pf. at 17.

623. This situation could apply to both customer accounts acquired by FairPoint and customer accounts remaining with Verizon. If the volume decreases, the price per circuit or service paid by customers could increase. Lafferty pf. at 17.

624. Requiring FairPoint to prorate the volume requirements to allow customers to receive the same benefits as prior to the Proposed Transaction will ensure that customers are treated the same as with Verizon. Lafferty pf. at 17.

b. Discussion

The Department requests that we ensure that FairPoint does not change any aspects of the tariffs, pricing, or other terms and conditions of service associated with access and other interconnection services. To the extent that FairPoint does need to make such changes, the Department seeks compensation for customers who must make modifications to their own systems. The Department also asks the Board to require FairPoint to prorate individual intrastate special access services as though the services were provided jointly by Verizon and FairPoint. The Department recommends that these requirements remain in place until the Board reviews the Incentive Regulation Plan in 2010.

FairPoint has agreed to all of these requests, except for the need to provide compensation. In particular, FairPoint will not seek a rate increase for special access service to be effective before three years after the merger closing date. For the same period, FairPoint will not seek to withdraw special access service offerings.[310] And, as discussed above concerning tariffs (in Part V.D.1.) and interconnection, FairPoint will prorate volumes for both tariffs and interconnection agreements so that customers are not harmed as a result of the tariffs.

On the question of compensation to customers, we addressed this issue in the context of FairPoint's changes to its systems and cutover. We found that FairPoint should not be required to pay compensation, although we will permit individual carriers to petition the Board to require compensation in extreme circumstances. That conclusion shall apply as well to special access circuits.

VI. CONCLUSION

For the reasons stated above, the Board denies the petition filed by FairPoint and Verizon, under which FairPoint would acquire the Vermont local-exchange and long-distance businesses (and related assets and operations) of Verizon.

While there are many appealing aspects to allowing FairPoint to replace Verizon, the evidence raises significant questions about FairPoint's financial soundness if this transaction were to close. Under reasonably foreseeable circumstances, FairPoint may face a difficult choice between maintaining a dividend to its shareholders and spending the money on operating expenses. Under one foreseeable scenario, FairPoint may even be unable to generate sufficient money to meet its large debt obligations. We have been unable to develop conditions that would ensure sufficient operating and capital funds to FairPoint's operating unit in Vermont, including

310. *See* Skrivan reb. pf. at 19. In testimony, FairPoint's witness agreed to these commitments for a period of 18 months. In the CLEC Settlement and on brief, FairPoint extended the commitments to three years.

its needs for capital to deploy broadband and achieve service quality standards. Therefore we disapprove the petition, in its current form.

But for these financial risks, we would approve the merger. Therefore, we will leave this docket open for a period of time to allow FairPoint and Verizon to modify their proposal. If we were to approve the merger, we would likely impose an extensive set of conditions that are necessary to ensure that the transaction would promote the public good and not impair competition. To guide FairPoint and Verizon and to expedite subsequent consideration, we have summarized those conditions in Appendix B. Notably, that list includes the "consistent coverage" broadband expansion plan proposed by the Department of Public Service.

VII. Order

It Is Hereby Ordered, Adjudged and Decreed by the Public Service Board of the State of Vermont that:

1. Pursuant to 30 V.S.A. §§ 107, 109 and 231, the proposed transfer of local exchange and long distance businesses of Verizon New England Inc., d/b/a Verizon Vermont, NYNEX Long Distance Company, Verizon Select Services Inc., and Bell Atlantic Communications, Inc. in Vermont to Northern New England Telephone Operations Inc. and Enhanced Communications of Northern New England Inc. and the transactions contemplated by the Merger Agreement are denied.

Dated at Montpelier, Vermont, this 21st day of December, 2007.

s/ James Volz	)	
	)	PUBLIC SERVICE
	)	
s/ David C. Coen	)	BOARD
	)	
	)	OF VERMONT
s/ John D. Burke	)	

A TRUE COPY:
OFFICE OF THE CLERK

FILED: DECEMBER 21, 2007

ATTEST: s/ Susan M. Hudson
Clerk of the Board

NOTICE TO READERS: This decision is subject to revision of technical errors. Readers are requested to notify the Clerk of the Board (by e-mail, telephone, or in writing) of any apparent errors, in order that any necessary corrections may be made. (E-mail address: psb.clerk@state.vt.us)

Appeal of this decision to the Supreme Court of Vermont must be filed with the Clerk of the Board within thirty days. Appeal will not stay the effect of this Order, absent further Order by this Board or appropriate action by the Supreme Court of Vermont. Motions for reconsideration or stay, if any, must be filed with the Clerk of the Board within ten days of the date of this decision and order.

APPENDIX A - GLOSSARY

Act	the Federal Telecommunications Act of 1996
ATM	Asynchronous Transfer Mode
BACI	Bell Atlantic Communications, Inc.
BOC	Bell Operating Company
C2C	Carrier-to-Carrier
Capgemini	Capgemini U.S. LLC
CLEC	Competitive Local Exchange Carrier
Comcast	Comcast Phone of Vermont, LLC
CPG	Certificate of Public Good
CRM	Customer Relationship Management
Department or DPS	Department of Public Service
DSL	Digital Subscriber Line
E911	Enhanced 911 service
EBITDA	Earnings before interest, taxes, depreciation, and amortization
Eight Independents	Shoreham Telephone Company, Inc., Topsham Telephone Company, Inc., Waitsfield-Fayston Telephone Company, Inc., d/b/a Waitsfield Telecom and d/b/a Champlain Valley Telecom; Northfield Telephone Company; Perkinsville Telephone Company; Ludlow Telephone Company; Franklin Telephone Company; and Vermont Telephone Company, Inc., d/b/a VTel
ETC	Eligible Telecommunications Carrier
FairPoint	FairPoint Communications, Inc.
FCC	Federal Communications Commission
FTTH	Fiber To The Home
GTE.net	GTE.net LLC
ILEC	Incumbent Local Exchange Carrier

I&M	Installation and maintenance
Incentive Regulation Plan	Verizon's 2005-2010 Amended Incentive Regulation Plan
ISP	Internet Service Provider
IP	Internet Protocol
IP/MPLS	Internet Protocol/Multiple Protocol Label Switching
IPTV	Internet Protocol Television
IT	Information Technology
KPI	Key Performance Indicator
Labor	The Communications Workers of America and the International Brotherhood of Electrical Workers
LEC	Local Exchange Carrier
Level 3	Level 3 Communications, LLC
LIBOR	London Interbank Offered Rate
LMS	Local Measured Service
LNP	Local Number Portability
MSAN	Multi-Service Access Nodes
MVNO	Mobile Virtual Network Operator
MOU	Memorandum of Understanding
NECTA	New England Cable and Telecommunications Association, Inc.
Newco	Enhanced Communications of Northern New England, Inc.
NNE	the Northern New England properties that FairPoint seeks to acquire
NYNEX Long Distance	NYNEX Long Distance Company
One Communications	One Communications Corp.
OSS	Operations Support System
PAP	Performance Assurance Plan
Plan	Alternative Regulation Plan

RMT	Reverse Morris Trust
SCP	Signal Control Point
segTEL	segTEL, Inc.
SGAT	Statements of Generally Available Terms and Conditions
SONET	Synchronous Optical Network
Sovernet	Sovernet, Inc.
Spinco	Northern New England Spinco, Inc.
SQ Plan	Service Quality Plan
SS7	Signaling System 7
Steady State Scenario	A financial FairPoint scenario with a constant rate of access line loss
STP	Signal Transfer Point
Telco	Northern New England Telephone Operations Inc.
TSA	Transition Services Agreement
TSR	Total Service Resale
UNE	Unbundled Network Element
UNE-P	UNE Platform
USF	Universal Service Fund
Verizon	Verizon New England Inc., d/b/a Verizon Vermont
VEC	Vermont Electric Cooperative, Inc.
VIT	Vermont Interactive Television
VoIP	Voice over Internet Protocol
VoIP Scenario	A financial FairPoint scenario with a constant rate of access line loss and additional losses due to cable VoIP
VSSI	Verizon Select Services Inc.
WOSS	Wholesale Operations Support System

<u>Appendix B</u>

The following are the conditions that would be adopted in any order approving the Proposed Transaction.

1. Subject to the conditions set out in this Order, the proposed transfer of local exchange and long distance businesses of Verizon New England Inc., d/b/a Verizon Vermont ("Verizon"), NYNEX Long Distance Company ("NYNEX Long Distance"), Verizon Select Services Inc. ("VSSI"), and Bell Atlantic Communications, Inc. ("BACI") in Vermont to Northern New England Telephone Operations Inc. ("Telco") and Enhanced Communications of Northern New England Inc. ("Newco") and the transactions contemplated by the Merger Agreement will promote the general good of the State of Vermont and are approved pursuant to 30 V.S.A. §§ 107, 109 and 231, and therefore a Certificate of Consent under 30 V.S.A. § 109 shall be issued.

2. The ownership and operation by Telco and Newco of their respective regulated businesses in Vermont, subject to the conditions in this Order, will promote the general good of Vermont and pursuant to 30 V.S.A. § 231, certificates of public good shall be issued to Telco and Newco.

3. Telco shall be designated as an Eligible Telecommunications Carrier ("ETC") pursuant to 47 U.S.C. § 254(e) and § 214(e)(2) for the service area previously designated for Verizon and Verizon may relinquish its designation as an ETC pursuant to 47 U.S.C. § 214(e)(4) and 47 C.F.R. § 54.205.

4. FairPoint shall continue to provide the nine services required of ETCs.

5. Subject to the conditions set out herein, the merger, and the acquisition by FairPoint of a controlling interest in Telco and Newco, will promote the public good, and the Board approves in all respects the transactions required or contemplated by the Merger Agreement, including the execution and performance by all parties of the Merger Agreement and all ancillary agreements and transactions required or contemplated by the Merger Agreement.

6. Subject to the conditions in this Order, the Merger will not result in obstructing or preventing competition in the purchase or sale of any product, service or commodity in the sale,

purchase or manufacture of which Verizon, NYNEX Long Distance, BACI, VSSI or FairPoint are engaged and is approved under 30 V.S.A. § 311.

7. Any abandonment and curtailment of regulated telecommunications services in Vermont by Verizon, NYNEX Long Distance, VSSI or BACI is consistent with the public interest, subject to Verizon's performance of continued obligations set out in this Order. At such time as the Board determines that Verizon has complied with the requirements of this Order relating to removal of dual poles, Verizon's Certificate of Public Good and/or equivalent authorization shall be revoked.

General Conditions

8. FairPoint shall appoint a senior level person with responsibility for communicating with the Board and Department. The person's primary place of business shall be in Vermont.

9. FairPoint shall provide the Board and Department updates on the FCC approval status for the license transfers under section 310(d) of the Federal Communications Commission's ("FCC") rules and the section 214 authorizations prior to closing. Approval of the acquisition is conditioned on FairPoint obtaining the required approvals from the FCC.

10. If FairPoint and Verizon receive conditional or unconditional regulatory approval from the FCC, the Maine Public Utilities Commission ("Maine PUC") or the New Hampshire Public Utility Commission ("NH PUC"), FairPoint and Verizon shall provide notice to the Board and Department of Public Service ("Department") and a copy of the relevant orders.

11. If regulatory approvals from the FCC, the Maine PUC or the NH PUC are conditional, approval in Vermont is conditioned upon subsequent review by this Board of the conditions imposed by those other regulatory bodies. The parties may not close the transaction until that subsequent Vermont review has been completed. The Board will provide an expedited procedure to review any such conditions.

Terms and Conditions of Service

12. FairPoint shall file tariffs, to be effective on the date of closing, that match the rates, terms and conditions in Verizon's current tariffs.

13. FairPoint shall be subject to the terms and conditions of the 2005–2010 Amended Incentive Regulation Plan (the "Incentive Regulation Plan") set out in Appendix A of the Board's Order of April 27, 2006, in Dockets 6959/7142 (including the 2005–2010 Amended Service Quality Plan set out in Appendix B), except as modified by this Order.

14. Through December 31, 2010, FairPoint shall not withdraw or increase the price on any regulated intrastate telecommunications service offered by Verizon under tariff as of the closing date of this transaction without the approval of the Board.

15. FairPoint shall prorate all volume pricing provided for in any tariff or other agreement so that the volume thresholds are reduced by the portion of the customer's volume that is generated in states outside of the acquired Verizon operations.

16. Notwithstanding any other provision of the Incentive Regulation Plan, the Board or the Department may seek rate reductions commensurate with any increase in Federal Universal Service Funding which the Vermont operation may be eligible to receive as a direct or indirect result of the transaction.

17. FairPoint shall assume Verizon's duty to provide annually a Performance Benchmark Report. FairPoint shall demonstrate that it has made arrangements to include all state-specific information currently described in that report.

18. FairPoint may not recover in rates any expenses related to the transaction or the transition from Verizon to FairPoint, including any acquisition premium or any increased costs which are due to FairPoint's need to develop and transition to new systems currently supported by Verizon, or which are incurred as a result of continued reliance on Verizon under the Transition Services Agreement.

<u>Broadband</u>

19. While meeting the statewide availability commitments for broadband set out in the Incentive Regulation Plan, FairPoint shall also provide broadband service to all access lines in at least 50% of its exchanges by the end of 2010.

a. As used in this condition, "Broadband" means a data transmission rate of not less than 1.5 Mbps per second in at least one direction.

b. FairPoint shall determine which exchanges it will serve with 100% broadband availability and publicly announce these exchanges as soon as possible after closing. Each exchange shall be contiguous with at least one other exchange (served by FairPoint or another company) with actual or planned 100% broadband availability.

20. Additional lines or line equivalents qualified for broadband service in the territory served out of the Burlington Central Office after July 1, 2005, shall be excluded from the number of additional lines qualified for broadband service for purposes of the calculations under the Incentive Regulation Plan.

Service Quality

21. FairPoint shall track on a monthly basis, Trouble Report Rates and Troubles Not Cleared in 24 Hours by exchange, and ensure that no exchange has a rate on any of these measures that exceeds twice the statewide standard. In addition, if the trouble report rate for any given wire center exceeds twice the statewide standard of 1.4 for three consecutive months, FairPoint shall develop a remediation plan to address the issues causing the higher trouble rate and file it with the Board and Department. Within 12 months of closing, FairPoint also shall develop and file with the Board and Department, an action plan for analysis and remediation of service quality issues for wire centers (other than those already addressed) where the trouble report rates have exceeded twice the statewide standard for at least three consecutive months.

22. If FairPoint fails to meet the performance baseline for the same service quality standard in three consecutive years, it shall file with the Board and Department an evaluation of the reasons for not meeting that standard and the proposed corrective actions.

23. FairPoint shall perform on all of Verizon's obligations under the settlement in Docket 6957.

24. FairPoint shall complete any of the improvement projects that Verizon has identified to address localized service quality issues if Verizon has not completed those projects by the date the parties close the transactions.

25. Prior to conversion, FairPoint shall provide the Department with the codes to be used in the new trouble tracking system to ensure the codes will provide the same information as reported by Verizon, and ensure that the codes map to the Verizon system used as a basis for the report.

26. Within six months of closing, FairPoint shall report on: (1) progress in establishing a tracking system for new customer service requests; (2) whether it has established a goal reflecting good service; (3) the percentage of customer service requests meeting that goal, by month; and (4) a narrative describing improvements that have been made in joint operations with electric utilities when responding to requests for new service.

27. FairPoint shall provide a detailed management plan that addresses quality and service issues before the acquisition is approved. The plan should address the following.

- Organizational Structure and responsibility
- Implementing a regimented approach to the inspection of work
- Quality policies and metrics
- Process flow – engineering, construction, testing, service provisioning
- Reducing error rate
- On time completion rate
- Training employees
- Analysis of data and improvement

Financial

28. FairPoint shall form a separate legal entity within the State of Vermont to separate all Vermont-related assets and liabilities, if any, from the assets and liabilities of other FairPoint regulated and non-regulated operations.

Regulation of FairPoint Vermont

29. The FairPoint Vermont lines shall be excluded from measurements of progress toward the Incentive Regulation Plan's broadband deployment milestones.

30. The election of FairPoint Vermont under 30 V.S.A. Section 227d is terminated; FairPoint Vermont shall be included in the provisions of the Incentive Regulation Plan related to changes in pricing, terms, and conditions of service.

31. FairPoint Vermont shall comply with the Annual Investment requirement of the Incentive Regulation Plan.

Poles

32. All dual poles shall be inventoried and a detailed work plan established within six months of closing.

33. All dual poles existing on the date of closing within Verizon's service area shall be removed by Verizon within 12 months of closing.

34. Before closing, Verizon shall establish an Overdue Pole Work Escrow Fund of $6,700,000 with a neutral administrator. The fund shall be available to FairPoint to compensate it for costs associated with removing the dual poles, using procedures designed to give Verizon reasonable opportunity to perform pole removal work using its own resources. The balance, with interest, shall be refunded when FairPoint certifies that the work has been completed.

Emergency Response

35. FairPoint shall adopt written emergency protocols for each electric utility in its serving area. The protocols shall be filed at the Board and Department by closing. If possible, the protocols shall be jointly adopted with the relevant electric utility.

36. No later than six months after closing, FairPoint shall file a demonstration that it has used its best efforts to enter into mutual aid agreements with comparably-sized or larger carriers in case of a natural disaster or other widespread emergency and file copies of any agreements that it has entered.

Cutover and Transition

37. FairPoint shall hire an Independent Monitor acceptable to it and to the Department. The scope of work, which shall be developed jointly by the Department and FairPoint, would include:

- Review and assessment of FairPoint planned testing and cutover readiness process, including a review of staffing requirements and plans, training plans and schedules, business readiness and the concerns and requirements expressed by wholesale systems users;
- Monitoring of testing and cutover readiness process;
- Pre-cutover readiness review and final report;
- Post-cutover review and report; and
- State regulator reporting and oversight.

38. The Independent Monitor will generate key deliverables, including draft final reports for review by the Board and interested parties, and will participate in a status conference with the Board, prior to cutover, to present and answer questions from the Board on FairPoint's cutover readiness.

39. Until FairPoint is obliged to give notice to Verizon to activate cutover on a specific date, the Board may order that cutover be delayed, if it has substantial concerns about FairPoint's readiness.

40. The cost of retaining the Independent Monitor shall be divided equally between FairPoint and Verizon.

41. FairPoint shall conduct a post-cutover "switch to bill to tariff" comparison to determine the accuracy of the converted billing records. This review shall involve sampling the customer base represented on multiple representative switches to determine the degree to which products that are provisioned on the switch are actually being billed to the customer, and that the products that are being billed to the customer meet the tariff requirements. The review should examine not only the accuracy of the conversion, but also the accuracy of the current switch profiles, and the quality of the source billing data as it relates to the switches and tariffs. The review shall be completed no later than nine months after cutover and filed with the Board and parties to this docket.

42. FairPoint shall conduct a billing audit within six months of cutover. The audit will be a statistically valid sampling of representative billing output from multiple billing cycles. This review would include full invoice verification. FairPoint may perform the audit in conjunction

with the "switch to bill to tariff" comparison and standard revenue operations production reviews.

43. FairPoint shall create a plan within 10–12 months after closing to transition and train Verizon employees, who are accustomed to Verizon's procedures, into FairPoint's operational processes. FairPoint shall establish its own written policies and procedures. FairPoint shall file these policies and procedures along with the transition plan.

44. During any of the first 18 monthly bills sent to customers under the new FairPoint billing systems, in each month in which the bill provided contains an error FairPoint shall provide each retail customer a credit of $5.00 (in addition to refunding any over-billing).

45. The Independent Monitor established to ensure FairPoint's system conversion process is implemented in a manner which eliminates risk to customers should include as one of its criteria an assurance that FairPoint's systems comply with the market opening requirements of the 1996 Act.

Competition

46. FairPoint shall be an incumbent local exchange carrier ("ILEC") subject to all of the obligations of Section 251 of the Federal Telecommunications Act of 1996 (the "Act"), including but not limited to the obligation to provide access to unbundled network elements (UNEs) wherever "impairment" exists pursuant to Sections 251(c)(3) and 251(d)(2)(B) of the Act, and the requirement to abide by the negotiation/arbitration process prescribed in section 252 of the Act.

47. FairPoint shall not seek or assert "rural telephone company" classification for FairPoint for purposes of the Section 251(f)(1) rural exemption from Section 251(c) of the Act. This condition does not prevent FairPoint from seeking or accepting designation of FairPoint as "rural" solely for purposes of qualifying for universal service funding or similar support from federal or state programs.

48. FairPoint shall not now or in the future seek any suspension or modification of any of FairPoint's 251(b) or (c) obligations pursuant to Section 251(f)(2) of the Act. This includes FairPointi's local number portability obligations under Section 251(b)(2).

49. For three years following the closing date of the Merger, FairPoint shall not reclassify as non-impaired any of FairPoint's wire centers in Vermont that are not currently classified as non-impaired. Thereafter, FairPoint shall provide separate notice if and when it decides to withdraw unbundled access to such transport in accordance with applicable tariff, contractual and regulatory notice requirements.

50. FairPoint shall adopt all of Verizon's interconnection agreements and other contracts. Where a contract cannot be adopted, FairPoint shall implement contracts that mirror the rates, terms and conditions in Verizon's contracts.

51. FairPoint shall adopt the Statement of Generally Available Terms ("SGAT") in effect as of the Merger closing date and the Vermont SGAT shall remain in place with rates capped at then-current levels for three years following the Merger closing date. Services available pursuant to said SGAT, as may be amended from time to time in accordance with applicable law (including the conditions in this Order) shall be made available to the competitive local exchange carriers ("CLEC") in accordance with the terms thereof.

52. All services offered to wholesale customers including CLECs under contract, the SGAT or tariffs by Verizon prior to close shall be continued under the same rates, terms and conditions and following the same processes by FairPoint.

53. FairPoint shall extend in writing all inter-carrier agreements in effect as of the Merger closing date for three years following their stated expiration date. Such extension shall not affect the right of a CLEC to terminate an agreement pursuant to the agreement's provisions. Either party may commence negotiation of a new agreement within nine months prior to the expiration of such extended term.

54. For agreements that have expired or are renewed only on a month-to-month basis as of the Merger closing date, FairPoint shall extend the then-current rates and other terms in writing for three years following the Merger closing date. Such extension shall not affect the right of either party to extend such agreements further on a month-to-month basis following the expiration of such three-year term, if the terms of the agreement permit such unilateral month-to-month extensions. Either party may commence negotiation of a new agreement within nine months prior to the expiration of the three-year extension term.

55. FairPoint shall cause all volume pricing provided for in either type of agreement described above, or in tariff-based volume discount programs, to be pro-rated so such volume pricing terms will be deemed to exclude volume requirements from states outside of the three-state area served by FairPoint following the Merger closing date. FairPoint shall work with CLECs and Verizon to provide them the same benefits in the aggregate as those provided by the existing Verizon volume discount arrangement; however, in the event that a CLEC chooses to reduce its spending in the FairPoint service territory post-closing, FairPoint is not required to hold such CLEC "harmless" in the amount of credit it receives under such volume discount arrangement.

56. FairPoint shall offer three-year agreements for tandem transit service, with rates capped at the current tandem transit rates for wholesale customers that agree to a three-year minimum term commitment.

57. FairPoint shall comply with number porting intervals and trunk ordering rules and intervals as may be set forth within existing tariffs, interconnection agreements or other agreements, as the case may be. Otherwise, FairPoint shall comply with industry standard number porting intervals and trunk ordering rules and intervals.

58. FairPoint shall provide as "Settlement Items" all Section 271(c)(2)(B) "competitive checklist" network elements and services to the extent that the FCC rules or has ruled that Bell Operating Companies ("BOCs") in general are required to provide such elements and services, now or in the future, at rates, terms and conditions that are just and reasonable, and not unreasonably discriminatory, as if governed by Sections 201(b) and 202(a) of the Act as interpreted by the FCC, subject to the rights of negotiation and of review set forth in the subsection below. If the U.S. Supreme Court should reverse the decision of the U.S. Court of Appeals for the First Circuit in *Verizon New England, Inc. v. Maine Public Utilities Commission*, Case Nos. 06-2151, 06-2429 (slip op. Sept. 6, 2007), then FairPoint will provide as "Settlement Items" such Section 271(c)(2)(B) elements and services as BOCs generally may be required to provide under applicable law. In the event the FCC through a final order delegates to the State of Vermont or the State of New Hampshire the authority to determine what elements and services must be provided by BOCs under Section 271(c)(2)(B), then this condition shall be

modified accordingly. Nothing herein shall limit the right of FairPoint or any of the parties to the CLEC Settlement to seek reconsideration or review of any such FCC order.

a. FairPoint may cease providing any Settlement Item in the event that the FCC, a state utility regulatory commission or a court (in each case having competent jurisdiction and authority) (each a "Governmental Authority") determines that such item is not required to be provided pursuant to applicable law.

b. In the event a CLEC requests in writing that FairPoint provide in Vermont a Settlement Item required to be provided under this condition, and not the subject of a determination described in subparagraph a, FairPoint and the CLEC will engage in good faith negotiations to reach agreement on the rates, terms and conditions pursuant to which FairPoint will provide such Settlement Item. In the event that FairPoint and the requesting CLEC are unable to reach agreement within nine months from the date FairPoint receives such written request, the CLEC shall have the right to seek resolution of any disputed rates, terms or conditions from the Board. The FCC's rules, regulations, orders and policies applicable to the definition of the corresponding item under Section 271(c)(2)(B) of the Act and the rates, terms and conditions at which such item must be provided by BOCs shall govern the Board's determinations in any such dispute resolution proceeding. Each Party to such dispute shall have the right to seek review in a court of competent jurisdiction of any state utility regulatory commission action relative to any Settlement Item, including any state utility regulatory commission order asserting that FairPoint is required to provide an element or service pursuant to this condition above, or setting rates, terms or conditions or asserting a pricing standard for any Settlement Item. None of the Parties will challenge the jurisdiction of the court of competent jurisdiction in which the dispute arises to apply FCC precedent to decide any such review proceeding that may be initiated hereunder. In addition, in any such review proceeding, none of the parties to the CLEC Settlement will challenge the jurisdiction of the state utility regulatory commission to resolve disputes over Settlement Items as provided in this subsection provided that the parties have first engaged in good faith negotiations as required herein, and provided further that in any such dispute resolution process the state applies the FCC's rules, regulations, orders and policies applicable to the definition of the corresponding item under Section 271(c)(2)(B) of the Act and the rates, terms and conditions at which such item must be provided by BOCs as agreed herein (or such alternative body of law, if any, as may be identified by the U.S. Supreme Court if that court should reverse the decision of the U.S. Court of Appeals for the First Circuit in Verizon New England, Inc. v. Maine Public Utilities Commission, Case Nos. 06-2151, 06-2429 (slip op. Sept. 6, 2007)).

59. For a period of three years following closing, FairPoint shall provide wholesale DSL and line sharing where available (provided that the purchaser employs non-interfering technology), subject to the following conditions.

a. FairPoint will provide wholesale DSL solely for the purpose of a CLEC's provision of end-user DSL service for three years following the Merger closing date, at a rate not to exceed 82% of FairPoint's lowest-priced retail rate advertised for stand-alone residential DSL service in Vermont.

b. At the CLEC's option, FairPoint shall provide line sharing either (A) at rates set in existing agreements, for the duration of the respective agreements and for an extended term expiring on the date which is three years following their stated expiration date (or three years following the Merger closing date in the case of agreements that remain in effect on a month-to-month basis as of the Merger closing date) at the price specified in the applicable agreement, or (B) for a period of three years following the Merger closing date (pursuant to a tariff provision providing that the offering shall expire by its own terms upon the expiration of such three-year period, unless FairPoint voluntarily extends the term) at a tariffed rate of $30.00 per line (non-recurring charge), plus a recurring charge of $6.00 per line per month (non-recurring charges will apply only to lines for which line sharing is not being provided by Verizon as of the Merger closing date).

c. FairPoint's offering of wholesale DSL or line sharing does not constitute its agreement that these services are required to be offered by BOCs under Section 271(c)(2)(B) of the Act or as a result of FairPoint's commitment to provide Settlement Items; if it should be determined that either offering is so required, the rates set out in this condition will constitute rates that are just and reasonable, and not unreasonably discriminatory, within the meaning of Section 201(b) and 202(a) of the Act and Condition 58 above, for the three-year term described herein.

d. FairPoint's obligations under this subsection are independent of any obligation FairPoint has to provide network elements or services under applicable law.

e. At the end of the three-year period referenced herein, FairPoint may, at its sole discretion, withdraw any offering of line sharing or wholesale DSL pursuant to this section that may then be in effect, including in any state tariff or SGAT. FairPoint will provide at least six months' advance notice of any withdrawal of line sharing or wholesale DSL, and the CLECs agree that such notice will constitute adequate and reasonable notice under applicable law.

60. FairPoint shall not file any new forbearance petition seeking relief from any of FairPoint's Section 251 obligations or obligations to provide access to Settlement Items in any wire center in Vermont for three years after the Merger closing date. FairPoint shall not be prohibited from pursuing rights of review or clarification or from enforcing any forbearance grant

arising from a prior Verizon petition. In such event, the three-year period following the Merger closing date shall constitute a reasonable transition period, and no CLEC shall seek any additional transition beyond such three-year period before FairPoint may give effect to any such forbearance authority.

61. FairPoint shall not file any new forbearance petition seeking non-dominant treatment for the acquired territory for three years after the Merger closing date. Nothing herein will restrict FairPoint from enforcing any forbearance from dominant carrier regulation already granted to Verizon (by operation of law or otherwise) in the acquired territory.

62. FairPoint shall comply with the requirements of Section 272(e) of the Act.

Performance Assurance Plan

63. FairPoint shall adopt and be subject to the Performance Assurance Plan ("PAP") that now applies to Verizon in Vermont. FairPoint shall adhere to the applicable PAP and Carrier-to-Carrier Guidelines in Vermont and shall be subject to the potential penalties and enforcement mechanisms set forth in those documents. The terms and conditions of the PAP shall remain in effect and applied to FairPoint until the Board orders a successor PAP. FairPoint has agreed not to challenge the Board's jurisdiction to enforce the PAP.

64. Any CLEC may seek enforcement of the PAP, even if such right is not expressly incorporated in the interconnection agreement, tariff or SGAT pursuant to which the CLEC purchases service.

65. After the Merger closing date, FairPoint shall work cooperatively with the CLECs and state utility regulatory staff in good faith to develop and implement a simplified, uniform PAP applicable to FairPoint in Maine, New Hampshire and Vermont. FairPoint agrees to begin this process by proposing for consideration by the CLECs a revised PAP that could be implemented in all three states.

66. FairPoint shall be responsible for the performance of all of FairPoint's wholesale OSS post-Cutover, in accordance with the terms of the PAP.

Miscellaneous Competitive Conditions

67. No later than six months after closing, FairPoint shall, after consultation with its wholesale customers file a proposal to the Board for a "Rapid Response Team" to address issues with wholesale customers arising from the transition from Verizon to FairPoint.

68. FairPoint shall identify the account team or single point of contact assigned to each CLEC.

69. FairPoint shall not pass through to CLECs any acquisition expenses, fees and expenses under the Transition Services Agreement ("TSA") or training expenses incurred by FairPoint in connection with the Merger or the transition to new operating systems. FairPoint reserves the right to seek inclusion in future FairPoint rate cases and cost studies (including but not limited to a future UNE rate proceeding) those capitalized costs arising out of development of new systems which replace systems used as of the Merger closing date by Verizon or its affiliates (including those replacing systems Verizon obtains from third parties), subject to normal review and regulation by the applicable state utility regulatory commission. Nothing herein constitutes an admission by any of the CLECs that FairPoint is entitled to any inclusion of such costs in its future rates or costs.

70. FairPoint shall provide, without charge, training in accordance with the training plan that it develops in accordance with Attachment 1 to the Stipulated Settlement Terms among FairPoint and certain CLECs filed with the Board. FairPoint shall continue to make available to CLECs the types of information that Verizon currently maintains and disseminates to CLECS regarding Verizon's systems and business rules and practices, including the CLEC Manual, industry letters and the change management process. Any CLEC that currently does not receive such materials (for example, because it takes service from the wholesale tariff without an interconnection agreement) may receive such materials upon request. FairPoint shall maintain the CLEC user forum process currently employed by Verizon.

71. FairPoint shall arrange a meeting with wholesale customers approximately six months following cutover to discuss customer concerns and questions. Meeting participants will be expected to inform FairPoint of concerns and questions in advance of the meeting so as to enable FairPoint to respond at or before the meeting.

72. FairPoint shall not request any increase in any of its tariffed rates for interstate or intrastate tariffed special access circuits to be effective within the three years following the Merger closing date, unless required by law. FairPoint may commence a proceeding or proceedings seeking an increase in such rates prior to the expiration of such three-year period provided that the effective date of the new rates shall not be before the end of such three-year period.

73. FairPoint shall not withdraw any of its currently tariffed interstate or intrastate offering of special access circuits offering for three years after the Merger closing date, unless required by law. This condition does not prevent FairPoint from withdrawing other services offered under the special access tariffs, including high-speed, packetized broadband services previously tariffed by Verizon but authorized by the FCC to be withdrawn from the interstate special access tariff.