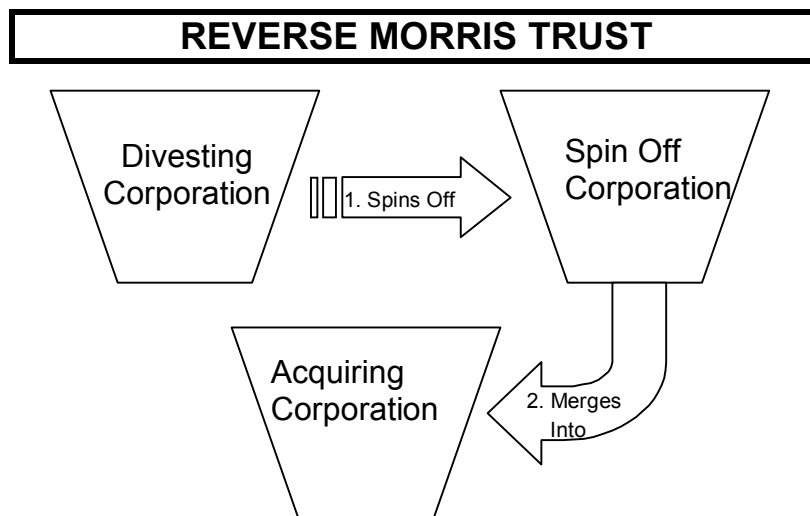


The Reverse Morris Trust Is Being Used by Verizon to Abandon its Customers and Avoid Taxes

The “Reverse Morris Trust” is a tax-avoidance technique that, thanks to Wall Street’s financial wizards, is increasingly deployed by corporations seeking to sell off unwanted assets without paying taxes on their gains. It is a remnant of the once-booming “disguised sale” transaction structure that many thought Congress had largely eliminated in the Taxpayer Relief Act of 1997.

Under a Reverse Morris Trust, a parent corporation can spin-off a subsidiary into an unrelated company, tax free, if the shareholders of the parent end up controlling more than 50% of the voting rights and economic value of the resulting merged company. The basic elements of this process are graphically described below: the Divesting Corporation creates a subsidiary Spin-Off Corporation which then merges into the unrelated Acquiring Corporation. To qualify for tax-free treatment, the divesting corporation’s shareholders (and thus the Spin Off Corporation as well) must own a controlling interest in the post-transaction Acquiring Corporation.

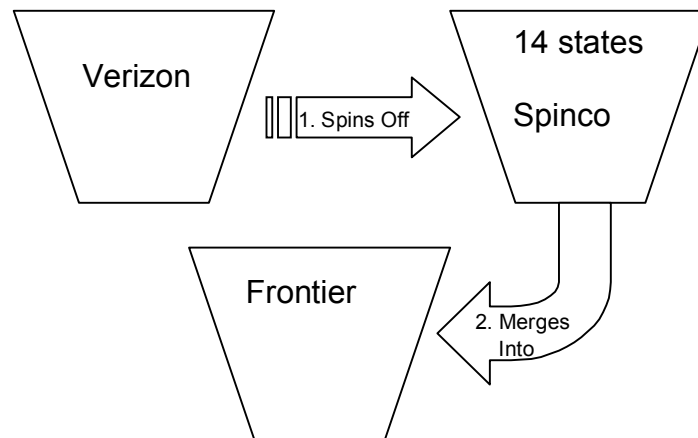


Typically, the parent loads up its “Spinco” with as much debt as it can support, while causing this subsidiary to “dividend-out” or otherwise pay the proceeds of the new debt to the parent or one of its affiliates immediately prior to the spin-off and merger.

Verizon Is Using the RMT to Abandon its Customers and Avoid Taxes. Verizon used the RMT to abandon its 1.7 million Northern New England customers and walk away with \$1.7 billion tax free. Meanwhile, FairPoint, the company to which Verizon sold these lines was unable to service its added debt and unable to transfer operations from Verizon.

Currently, Verizon is attempting to obtain regulatory approval for the proposed sale of its 4.8 million access lines in 14 states to Frontier, a much smaller acquisition firm with just 2.2 million access lines. The ONLY reason Verizon chose to sell to such a small company was to take advantage of the Reverse Morris Trust tax loophole. Here are the steps to the deal.

REVERSE MORRIS TRUST: Verizon-Frontier



1. Verizon finds a buyer that is smaller than the properties it wants to abandon. In this case, Frontier is the acquiring company.
2. Verizon spins-off its 14-state operations into a new subsidiary called Spinco which will borrow as much as possible. In this case, it is \$3.3 billion dollars.
3. Verizon then will require its Spinco subsidiary to pay Verizon a “dividend” equal to the cash it forced Spinco to borrow.
4. Verizon also will require Spinco to keep the IOU and commit to pay back the money it borrowed.
5. When the transaction is approved, Spinco will be merged into Frontier. Frontier will issue approximately \$5.3 billion in new stock to Verizon shareholders who will own about 70% of the post-merger Frontier.
6. This leaves the “new” company – in this case Frontier - buried in more debt, greater dividend commitments and less money to invest in new technology, much less maintain the existing infrastructure.
7. Meanwhile, this scheme saves Verizon millions in taxes that Verizon would pay if it sold to a larger company with the resources to invest in new technology and service quality. In the case of the sale to Frontier, Verizon will avoid paying an estimated \$600 million in taxes. In its previous sale to FairPoint, Verizon avoided paying an estimated \$300 million in taxes.

Congress should close the RMT loophole that actually subsidizes corporate transactions that eliminate good community jobs and place rural communities on an information dirt road, instead of the information super highway. No rural telecom job is safe as long as this loophole exists.