

VERIZON COMMUNICATIONS INC  
Form 10-Q  
May 04, 2007  
Table of Contents

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

(Mark one)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2007

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number 1-8606

**Verizon Communications Inc.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State of Incorporation)

**23-2259884**  
(I.R.S. Employer Identification No.)

**140 West Street**  
**New York, New York**  
(Address of principal executive offices)

**10007**  
(Zip Code)

**Registrant's telephone number (212) 395-1000**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

At March 31, 2007, 2,903,363,700 shares of the registrant's Common Stock were outstanding, after deducting 64,288,738 shares held in treasury.

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**Table of Contents****Table of Contents**

|   | <b>Page</b> |
|---|-------------|
| <b>Part I. <u>Financial Information</u></b>   |             |
| <b>Item 1. <u>Financial Statements (Unaudited)</u></b>  |             |
| <b><u>Condensed Consolidated Statements of Income</u></b>   |             |
| <i>Three months ended March 31, 2007 and 2006</i>   | 1           |
| <b><u>Condensed Consolidated Balance Sheets</u></b>   |             |
| <i>At March 31, 2007 and December 31, 2006</i>  | 2           |
| <b><u>Condensed Consolidated Statements of Cash Flows</u></b>   |             |
| <i>Three months ended March 31, 2007 and 2006</i>   | 3           |
| <b><u>Notes to Condensed Consolidated Financial Statements</u></b>  | 4           |
| <b>Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></b> | 19          |
| <b>Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u></b>                            | 41          |
| <b>Item 4. <u>Controls and Procedures</u></b>   | 41          |
| <b>Part II. <u>Other Information</u></b>  |             |
| <b>Item 1. <u>Legal Proceedings</u></b>   | 41          |
| <b>Item 1A. <u>Risk Factors</u></b>   | 42          |
| <b>Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u></b>                           | 42          |
| <b>Item 6. <u>Exhibits</u></b>  | 42          |
| <b><u>Signature</u></b>   | 43          |
| <b><u>Certifications</u></b>  | 45          |

**Table of Contents****Part I - Financial Information****Item 1. Financial Statements****Condensed Consolidated Statements of Income**

Verizon Communications Inc. and Subsidiaries

**Three Months Ended March 31,**

(Dollars in Millions, Except Per Share Amounts) (Unaudited)

|   | <b>2007</b> | <b>2006</b> |
|---|-------------|-------------|
| <b>Operating Revenues</b>   | \$ 22,584   | \$ 21,231   |
| <b>Operating Expenses</b>   |             |             |
| Cost of services and sales (exclusive of items shown below)   | 8,912       | 8,516       |
| Selling, general and administrative expense   | 6,343       | 5,873       |
| Depreciation and amortization expense   | 3,533       | 3,667       |
| <b>Total Operating Expenses</b>   | 18,788      | 18,056      |
| <b>Operating Income</b>   | 3,796       | 3,175       |
| Equity in earnings of unconsolidated businesses   | 160         | 157         |
| Other income and (expense), net   | 48          | 103         |
| Interest expense  | (485)       | (636)       |
| Minority interest   | (1,154)     | (866)       |
| <b>Income Before Provision For Income Taxes, Discontinued Operations, Extraordinary Item and Cumulative Effect of Accounting Change</b> | 2,365       | 1,933       |
| Provision for income taxes  | (881)       | (651)       |
| <b>Income Before Discontinued Operations, Extraordinary Item and Cumulative Effect of Accounting Change</b>                             | 1,484       | 1,282       |
| Income from discontinued operations, net of tax   | 142         | 392         |
| Extraordinary item, net of tax  | (131)       |             |
| Cumulative effect of accounting change, net of tax  |             | (42)        |
| <b>Net Income</b>   | \$ 1,495    | \$ 1,632    |
| <b>Basic Earnings Per Common Share<sup>(1)</sup></b>  |             |             |
| Income before discontinued operations, extraordinary item and cumulative effect of accounting change                                    | \$ .51      | \$ .44      |
| Income from discontinued operations, net of tax   | .05         | .13         |
| Extraordinary item, net of tax  | (.05)       |             |
| Cumulative effect of accounting change, net of tax  |             | (.01)       |
| <b>Net Income</b>   | \$ .51      | \$ .56      |
| Weighted-average shares outstanding (in millions)   | 2,909       | 2,915       |

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**Diluted Earnings Per Common Share<sup>(1)</sup>**

|  |               |               |
|--|---------------|---------------|
| Income before discontinued operations, extraordinary item and cumulative effect of accounting change | \$ .51        | \$ .44        |
| Income from discontinued operations, net of tax  | .05           | .13           |
| Extraordinary item, net of tax   | (.05)         |               |
| Cumulative effect of accounting change, net of tax   |               | (.01)         |
| <b>Net Income</b>  | <b>\$ .51</b> | <b>\$ .56</b> |
| Weighted-average shares outstanding (in millions)  | 2,911         | 2,963         |
| Dividends declared per common share  | \$ .405       | \$ .405       |

<sup>(1)</sup> Total of per share amounts may not add due to rounding.  
See Notes to Condensed Consolidated Financial Statements

**Table of Contents****Condensed Consolidated Balance Sheets**

Verizon Communications Inc. and Subsidiaries

(Dollars in Millions, Except Per Share Amounts) (Unaudited)

**At March 31, 2007****At December 31, 2006**

| <b>Assets</b>  |           |                |                   |
|--|-----------|----------------|-------------------|
| Current assets   |           |                |                   |
| Cash and cash equivalents  | \$        | 1,301          | \$ 3,219          |
| Short-term investments   |           | 2,149          | 2,434             |
| Accounts receivable, net of allowances of \$1,153 and \$1,139                        |           | 10,177         | 10,891            |
| Inventories  |           | 1,780          | 1,514             |
| Assets held for sale   |           |                | 2,592             |
| Prepaid expenses and other   |           | 2,487          | 1,888             |
| <b>Total current assets</b>  |           | <b>17,894</b>  | <b>22,538</b>     |
| <br>   |           |                |                   |
| Plant, property and equipment  |           | 206,585        | 204,109           |
| Less accumulated depreciation  |           | 123,607        | 121,753           |
|  |           | 82,978         | 82,356            |
| <br>   |           |                |                   |
| Investments in unconsolidated businesses   |           | 4,898          | 4,868             |
| Wireless licenses  |           | 50,566         | 50,959            |
| Goodwill   |           | 5,247          | 5,655             |
| Other intangible assets, net   |           | 5,195          | 5,140             |
| Other assets   |           | 17,506         | 17,288            |
| <br>   |           |                |                   |
| <b>Total assets</b>  | <b>\$</b> | <b>184,284</b> | <b>\$ 188,804</b> |
| <br>   |           |                |                   |
| <b>Liabilities and Shareowners Investment</b>  |           |                |                   |
| Current liabilities  |           |                |                   |
| Debt maturing within one year  | \$        | 6,604          | \$ 7,715          |
| Accounts payable and accrued liabilities   |           | 13,309         | 14,320            |
| Liabilities related to assets held for sale  |           |                | 2,154             |
| Other  |           | 7,993          | 8,091             |
| <b>Total current liabilities</b>   |           | <b>27,906</b>  | <b>32,280</b>     |
| <br>   |           |                |                   |
| Long-term debt   |           | 28,073         | 28,646            |
| Employee benefit obligations   |           | 29,743         | 30,779            |
| Deferred income taxes  |           | 13,518         | 16,270            |
| Other liabilities  |           | 7,025          | 3,957             |
| Minority interest  |           | 29,237         | 28,337            |
| <br>   |           |                |                   |
| Shareowners investment   |           |                |                   |
| Series preferred stock (\$.10 par value; none issued)                                |           |                |                   |
| Common stock (\$.10 par value; 2,967,652,438 shares and 2,967,652,438 shares issued) |           | 297            | 297               |

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|  |                   |                   |
|--|-------------------|-------------------|
| Contributed capital  | 40,122            | 40,124            |
| Reinvested earnings  | 17,485            | 17,324            |
| Accumulated other comprehensive loss                           | (7,136)           | (7,530)           |
| Common stock in treasury, at cost                              | (2,185)           | (1,871)           |
| Deferred compensation employee stock ownership plans and other | 199               | 191               |
| <b>Total shareowners investment</b>                            | <b>48,782</b>     | <b>48,535</b>     |
| <b>Total liabilities and shareowners investment</b>            | <b>\$ 184,284</b> | <b>\$ 188,804</b> |

See Notes to Condensed Consolidated Financial Statements

**Table of Contents****Condensed Consolidated Statements of Cash Flows**

Verizon Communications Inc. and Subsidiaries

| (Dollars in Millions) (Unaudited)   | <b>Three Months Ended March 31,</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2007</b>                         | <b>2006</b> |
| <b>Cash Flows from Operating Activities</b>   |                                     |             |
| Net Income  | \$ 1,495                            | \$ 1,632    |
| Adjustments to reconcile net income to net cash provided by operating activities continuing operations: |                                     |             |
| Depreciation and amortization expense   | 3,533                               | 3,667       |
| Employee retirement benefits  | 430                                 | 481         |
| Deferred income taxes   | 222                                 | (149)       |
| Provision for uncollectible accounts  | 281                                 | 294         |
| Equity in earnings of unconsolidated businesses   | (160)                               | (157)       |
| Extraordinary item, net of tax  | 131                                 |             |
| Cumulative effect of accounting change, net of tax  |                                     | 42          |
| Changes in current assets and liabilities, net of effects from acquisition/disposition of businesses    | (1,116)                             | (382)       |
| Other, net  | 228                                 | 185         |
| Net cash provided by operating activities continuing operations   | 5,044                               | 5,613       |
| Net cash provided by (used in) operating activities discontinued operations                             | (527)                               | 453         |
| Net cash provided by operating activities   | 4,517                               | 6,066       |
| <b>Cash Flows from Investing Activities</b>   |                                     |             |
| Capital expenditures (including capitalized software)   | (4,163)                             | (4,021)     |
| Acquisitions, net of cash acquired, and investments   | (124)                               | 1,526       |
| Net change in short-term investments  | 282                                 | 433         |
| Other, net  | 61                                  | 313         |
| Net cash used in investing activities continuing operations   | (3,944)                             | (1,749)     |
| Net cash provided by investing activities discontinued operations                                       | 757                                 | 1           |
| Net cash used in investing activities   | (3,187)                             | (1,748)     |
| <b>Cash Flows from Financing Activities</b>   |                                     |             |
| Proceeds from long-term borrowings  | 1,424                               | 3,971       |
| Repayments of long-term borrowings and capital lease obligations  | (3,314)                             | (6,129)     |
| Increase in short-term obligations, excluding current maturities  | 141                                 | 14          |
| Dividends paid  | (1,179)                             | (1,185)     |
| Proceeds from sale of common stock  | 110                                 | 64          |
| Purchase of common stock for treasury   | (427)                               | (398)       |
| Other, net  | (3)                                 | (117)       |
| Net cash used in financing activities continuing operations   | (3,248)                             | (3,780)     |
| Net cash used in financing activities discontinued operations   |                                     | (50)        |
| Net cash used in financing activities   | (3,248)                             | (3,830)     |



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|  |          |          |
|--|----------|----------|
| Increase (decrease) in cash and cash equivalents | (1,918)  | 488      |
| Cash and cash equivalents, beginning of period   | 3,219    | 760      |
| Cash and cash equivalents, end of period         | \$ 1,301 | \$ 1,248 |

See Notes to Condensed Consolidated Financial Statements

**Table of Contents****Notes to Condensed Consolidated Financial Statements**

Verizon Communications Inc. and Subsidiaries

(Unaudited)

**1. Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared based upon Securities and Exchange Commission (SEC) rules that permit reduced disclosure for interim periods. These financial statements reflect all adjustments that are necessary for a fair presentation of results of operations and financial condition for the interim periods shown including normal recurring accruals and other items. The results for the interim periods are not necessarily indicative of results for the full year. For a more complete discussion of significant accounting policies and certain other information, you should refer to the financial statements included in the Verizon Communications Inc. (Verizon) Annual Report on Form 10-K for the year ended December 31, 2006.

We have reclassified prior year amounts to conform to the current year presentation.

**2. Discontinued Operations, Extraordinary Item and Sale of Businesses, net***Telecomunicaciones de Puerto Rico, Inc.*

On March 27, 2007, the Federal Communications Commission approved the sale of Telecomunicaciones de Puerto Rico, Inc. (TELPRI) to América Móvil, S.A.B. de C.V. (América Móvil). On March 30, 2007, we completed the sale and received gross proceeds of approximately \$980 million, \$100 million of which was contributed to the Verizon Foundation. The sale resulted in a pretax gain of \$120 million (\$70 million after-tax). América Móvil purchased 100% of TELPRI, the holding company of Puerto Rico Telephone Company, including Verizon's 52% interest.

In accordance with Statement of Financial Accounting Standard (SFAS) No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, we have classified the results of operations of TELPRI as discontinued operations in the consolidated statements of income for all periods presented through the date of the sale. The assets and liabilities of TELPRI are disclosed as assets held for sale and liabilities related to assets held for sale in the condensed consolidated balance sheets as of December 31, 2006. Additional detail related to those assets and liabilities were as follows:

| (Dollars in Millions)              | <b>At December 31, 2006</b> |              |
|------------------------------------|-----------------------------|--------------|
| Current assets                     | \$                          | 303          |
| Plant, property and equipment, net |                             | 1,436        |
| Other non-current assets           |                             | 853          |
| <b>Total assets</b>                | <b>\$</b>                   | <b>2,592</b> |
| Current liabilities                | \$                          | 181          |
| Long-term debt                     |                             | 575          |
| Other non-current liabilities      |                             | 1,398        |
| <b>Total liabilities</b>           | <b>\$</b>                   | <b>2,154</b> |

Related to the assets and liabilities above was \$241 million included as Accumulated Other Comprehensive Loss in the condensed consolidated balance sheets as of December 31, 2006.



**Table of Contents**

Income from discontinued operations, net of tax, for TELPRI, Verizon Dominicana and Verizon Information Services presented in the condensed consolidated statements of income was comprised of the following:

| (Dollars in Millions)                           | <b>Three Months Ended March 31,</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2007</b>                         | <b>2006</b> |
| Operating revenues                              | \$ 306                              | \$ 1,512    |
| Income before provision for income taxes        | \$ 185                              | \$ 618      |
| Provision for income taxes                      | (43)                                | (226)       |
| Income from discontinued operations, net of tax | \$ 142                              | \$ 392      |

*Compañía Anónima Nacional Teléfonos de Venezuela (CANTV)*

In January 2007, the Bolivarian Republic of Venezuela (the Republic) declared its intent to nationalize certain companies, including CANTV. On February 12, 2007, we entered into a Memorandum of Understanding (MOU) with the Republic. The MOU provides that the Republic will offer to purchase all of the equity securities of CANTV, including our 28.5% interest, through public tender offers in Venezuela and the United States at a price equivalent to \$17.85 per American Depository Share (ADS), subject to adjustment if CANTV declared and paid a dividend prior to the purchase of the equity securities in the tender offers. A dividend of 6,454.49 Bolivars per ADS (equivalent to \$3.00 at the current official exchange rate) with an April 18, 2007 payment date was recommended by the CANTV Board and then approved by shareholders on March 30, 2007. The Republic launched the public tender offers on April 9, 2007 at a price equivalent to \$14.85 per ADS. Unless extended, the offers will expire on May 8, 2007. The price is subject to further adjustment for any additional dividends declared and paid before the date the equity securities are accepted for payment, and in the event of a change in the official exchange rate, for changes to the equivalent dollar value of the April 18 dividend. The tender offers are subject to certain conditions including that a majority of the outstanding shares are tendered to the Republic. Based upon the terms of the MOU and our current investment balance in CANTV, we recorded an extraordinary loss on our investment of \$131 million, net of tax in the first quarter of 2007. If the tender offers are completed, Verizon expects to receive an aggregate amount of \$572 million through a combination of purchase price and the 2007 dividend.

*Telephone Access Lines Spin-off*

On January 16, 2007, we announced a definitive agreement with FairPoint Communications, Inc. (FairPoint) that will result in Verizon establishing a separate entity for its local exchange and related business assets in Maine, New Hampshire and Vermont, spinning off that new entity to Verizon's shareowners, and immediately merging it with and into FairPoint. These local exchange and business assets are included in Verizon's continuing operations. The transaction is subject to the satisfaction of certain conditions, including receipt of state and federal telecommunications regulatory approvals. We expect this transaction to close within one year of the date of announcement.

Upon the closing of the transaction, Verizon shareowners will own approximately 60 percent of the new company and FairPoint stockholders will own approximately 40 percent. Verizon Communications will not own any shares in FairPoint after the merger. In connection with the merger, Verizon shareowners will receive one share of FairPoint stock for approximately every 55 shares of Verizon stock held as of the record date. Both the spin-off and merger are expected to qualify as tax-free transactions, except to the extent that cash is paid to Verizon shareowners in lieu of fractional shares.

The total value to be received by Verizon and its shareowners in exchange for these operations will be approximately \$2,715 million. Verizon shareowners will receive approximately \$1,015 million of FairPoint common stock in the merger, based upon FairPoint's recent stock price and the terms of the merger agreement. Verizon will receive \$1,700 million in value through a combination of cash distributions to Verizon and debt securities issued to Verizon prior to the spin-off. Verizon may exchange these newly issued debt securities for certain debt that was previously issued by Verizon, which would have the effect of reducing Verizon's then-outstanding debt.

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**Table of Contents**

**3. Taxes**

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*FASB Interpretation No. 48*

Effective January 1, 2007, we adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48), which requires the use of a two-step approach for recognizing and measuring tax benefits taken or expected to be taken in a tax return and disclosures regarding uncertainties in income tax positions. As a result of the implementation of FIN 48, we recorded adjustments to liabilities that resulted in a net \$79 million increase in the liability for unrecognized tax benefits with an offsetting reduction to retained earnings as of January 1, 2007. The implementation of FIN 48 also resulted in adjustments to prior acquisitions accounted for under purchase accounting, resulting in a \$635 million reduction in the liability for unrecognized tax benefits and corresponding reductions to goodwill and wireless licenses of \$100 million and \$535 million, respectively. The implementation impact included a reduction in Deferred income taxes of approximately \$3 billion, offset with a similar increase in Other liabilities as of January 1, 2007.

The total amount of unrecognized tax benefits at January 1, 2007 is \$2,958 million. Included in the total unrecognized tax benefits is \$1,290 million that, if recognized, would favorably affect the effective tax rate. The remaining unrecognized tax benefits relate to temporary items that would not affect the annual effective tax rate and uncertain tax positions resulting from prior acquisitions which, pursuant to current purchase accounting tax rules, would adjust goodwill.

We recognize any interest and penalties accrued related to unrecognized tax benefits in income tax expense. We had approximately \$444 million (after-tax) for the payment of interest and penalties accrued in the balance sheet at January 1, 2007, relating to the \$2,958 million unrecognized tax benefits reflected above. We had approximately \$486 million (after-tax) for the payment of interest and penalties accrued in the balance sheet at March 31, 2007.

Verizon or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction, and various state and local and foreign jurisdictions. The Company is generally no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2000. The Internal Revenue Service (IRS) is currently examining the Company's U.S. income tax returns for years 2000 through 2003. We do not anticipate any significant increase or decrease to the unrecognized tax benefits within the next twelve months.

*FASB Staff Position FAS 13-2*

FASB Staff Position FAS 13-2, *Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction* (FSP 13-2) requires that changes in the projected timing of income tax cash flows generated by a leveraged lease transaction be recognized as a gain or loss in the year in which the change occurs. We adopted FSP 13-2 effective January 1, 2007. The cumulative effect of initially adopting FSP 13-2 was a reduction to retained earnings of \$55 million, after-tax. There was no impact on our condensed consolidated income statement.

**4. Completion of Merger with MCI**

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On January 6, 2006, after receiving the required state, federal and international regulatory approvals, Verizon completed the acquisition of 100% of the outstanding common stock of MCI, Inc. (MCI) for a combination of Verizon common shares and cash. MCI was a global communications company that provided Internet, data and voice communication services to businesses and government entities throughout the world and consumers in the United States.

The merger was accounted for using the purchase method in accordance with SFAS No. 141, *Business Combinations*, and the aggregate transaction value was \$6,890 million, consisting of the cash and common stock issued at closing (\$5,829 million), the consideration for the shares acquired from the Carlos Slim Helú entities, net of the portion of the special dividend paid by MCI that was treated as a return of our investment (\$973 million) and closing and other direct merger-related costs. The number of shares issued was based on the Average Parent Stock Price, as defined in the merger agreement. The consolidated financial statements include the results of MCI's operations from the date of the close of the merger.

**Table of Contents**

We recorded certain severance and severance-related costs and contract termination costs in connection with the merger, pursuant to the Emerging Issues Task Force Issue No. 95-3, *Recognition of Liabilities in Connection with a Purchase Business Combination*. The remaining severance and severance-related costs will be paid in 2007, and the remaining contract termination costs will be paid over the remaining contract periods through 2009. The following table summarizes the activity related to these obligations during 2007:

| (Dollars in Millions)                               | At December 31, 2006 | Payments | At March 31, 2007 |
|---|----------------------|----------|-------------------|
| Severance costs and contract termination costs      | \$ 376               | \$ (256) | \$ 120            |
| <b>5. Strategic Actions and Other Special Items</b> |                      |          |                   |

During the first quarter of 2007, we recorded pretax charges of \$14 million (\$9 million after-tax) related to systems integration activities associated with the MCI acquisition, and, as a result of the sale of TELPRI, Verizon contributed \$100 million to Verizon Foundation to fund its charitable activities and increase its self-sufficiency.

During the first quarter of 2006, we recorded pretax charges of \$55 million (\$35 million after-tax) related to integration costs associated with the MCI acquisition that primarily comprised of advertising and other costs related to re-branding initiatives and systems integration activities. Also during the first quarter of 2006, we recorded pretax charges of \$46 million (\$28 million after-tax) in connection with the continued relocation of employees and business operations to Verizon Center located in Basking Ridge, New Jersey.

**6. Goodwill and Other Intangible Assets***Goodwill*

Changes in the carrying amount of goodwill were as follows:

| (Dollars in Millions)               | Wireline | Domestic<br>Wireless | Total    |
|-------------------------------------|----------|----------------------|----------|
| <b>Balance at December 31, 2006</b> | \$ 5,310 | \$ 345               | \$ 5,655 |
| Reclassifications and adjustments   | (408)    |                      | (408)    |
| <b>Balance at March 31, 2007</b>    | \$ 4,902 | \$ 345               | \$ 5,247 |

Reclassifications and adjustments to goodwill during the first quarter of 2007 reflects revised estimated tax bases of acquired assets and liabilities, as well as adjustments related to the adoption of FIN 48 (see Note 3).

*Other Intangible Assets*

The following table displays the details of other intangible assets:

| (Dollars in Millions)                            | At March 31, 2007 |                             | At December 31, 2006 |                             |
|--|-------------------|-----------------------------|----------------------|-----------------------------|
|  | Gross<br>Amount   | Accumulated<br>Amortization | Gross<br>Amount      | Accumulated<br>Amortization |
| Finite-lived intangible assets:                  |                   |                             |                      |                             |
| Customer lists (3 to 8 years)                    | \$ 1,273          | \$ 309                      | \$ 1,278             | \$ 270                      |
| Non-network internal-use software (1 to 7 years) | 7,617             | 3,560                       | 7,777                | 3,826                       |

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|                       |          |          |          |          |
|-----------------------|----------|----------|----------|----------|
| Other (1 to 25 years) | 203      | 29       | 204      | 23       |
| <b>Total</b>          | \$ 9,093 | \$ 3,898 | \$ 9,259 | \$ 4,119 |

Indefinite-lived intangible assets:

|                   |           |           |
|-------------------|-----------|-----------|
| Wireless licenses | \$ 50,566 | \$ 50,959 |
|-------------------|-----------|-----------|

Wireless licenses reflected adjustments related to the adoption of FIN 48 (see Note 3), as well as acquisitions during the first quarter of 2007. Amortization expense was \$343 million and \$463 million for the three months ended March 31, 2007 and 2006 respectively. Amortization expense is estimated to be \$1,006 million for the remainder of 2007, \$1,174 million in 2008, \$973 million in 2009, \$749 million in 2010 and \$584 million in 2011.

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## **Table of Contents**

### **7. Debt**

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#### *Issuance of Debt*

In February 2007, Verizon drew down on a \$425 million floating rate vendor financing facility due 2013. In March 2007, Verizon issued \$1,000 million of 13-month floating rate exchangeable notes with an original maturity of 2008. These notes are exchangeable periodically at the option of the note holder into similar notes until 2017.

On March 29, 2007, Verizon agreed to issue an aggregate \$2,000 million of fixed and floating rate notes. On April 3, 2007, Verizon issued these notes, consisting of \$750 million of 5.50% notes due 2017, \$750 million of 6.25% notes due 2037, and \$500 million of floating rate notes due 2009 resulting in cash proceeds of \$1,978 million, net of discounts and issuance costs.

#### *Redemption of Debt*

Previously, Verizon issued \$1,750 million in principal amount at maturity of floating rate notes due August 15, 2007, which were callable by Verizon on or after August 15, 2006. On January 8, 2007, we redeemed the remaining \$1,580 million principal of the outstanding floating rate notes at a redemption price equal to 100% of the principal amount of the notes being redeemed plus accrued and unpaid interest on the principal amount of the notes being redeemed to the date of redemption. The total payment on the date of redemption was approximately \$1,593 million.

During the first quarter of 2007, the \$150 million GTE Southwest Inc. 6.23% notes and the \$275 million Verizon California Inc. 7.65% notes matured and were repaid. In addition, we redeemed the \$500 million of GTE Corporation 7.90% debentures due February 1, 2027 and the \$300 million Verizon South Inc. 7.0% debentures, Series F, due 2041 at various redemption prices plus accrued and unpaid interest to the redemption dates. We recorded pretax charges of \$28 million (\$18 million after-tax) in connection with the early extinguishments of this debt.

#### *Other Debt Extinguishment Costs*

We recorded pretax charges of \$26 million (\$16 million after-tax) during the first quarter of 2006 resulting from the extinguishment of debt assumed in connection with the completion of the MCI merger.

#### *Support Agreements and Guarantees*

All of Verizon Global Funding's debt had the benefit of Support Agreements between us and Verizon Global Funding, which gave holders of Verizon Global Funding debt the right to proceed directly against us for payment of interest, premium (if any) and principal outstanding should Verizon Global Funding fail to pay. The holders of Verizon Global Funding debt did not have recourse to the stock or assets of most of our telephone operations; however, they did have recourse to dividends paid to us by any of our consolidated subsidiaries as well as assets not covered by the exclusion. On February 1, 2006, Verizon announced the merger of Verizon Global Funding into Verizon. As a result of the merger, all of Verizon Global Funding's debt has been assumed by Verizon by operation of law.

In addition, Verizon Global Funding had guaranteed the debt obligations of GTE Corporation (but not the debt of its subsidiary or affiliate companies) that were issued and outstanding prior to July 1, 2003. In connection with the merger of Verizon Global Funding into Verizon, Verizon has assumed this guarantee. As of March 31, 2007, \$2,450 million principal amount of these obligations remained outstanding.

Verizon and NYNEX Corporation are the joint and several co-obligors of the 20-Year 9.55% Debentures due 2010 previously issued by NYNEX on March 26, 1990. As of March 31, 2007, \$92 million principal amount of this obligation remained outstanding. NYNEX and GTE no longer issue public debt or file SEC reports. See Note 13 for information on guarantees of operating subsidiary debt listed on the New York Stock Exchange.

#### *Debt Covenants*

We and our consolidated subsidiaries are in compliance with all of our debt covenants.



**Table of Contents****8. Earnings Per Share**

The following table is a reconciliation of the numerators and denominators used in computing basic and diluted earnings per share:

| (Dollars and Shares in Millions, Except Per Share Amounts)   | <b>Three Months Ended March 31,</b> |             |
|--|-------------------------------------|-------------|
|  | <b>2007</b>                         | <b>2006</b> |
| <b>Net Income Used For Basic Earnings Per Common Share</b>   |                                     |             |
| Income before discontinued operations, extraordinary item and cumulative effect of accounting change   | \$ 1,484                            | \$ 1,282    |
| Income from discontinued operations, net of tax  | 142                                 | 392         |
| Extraordinary item, net of tax   | (131)                               |             |
| Cumulative effect of accounting change, net of tax   |                                     | (42)        |
| Net income   | \$ 1,495                            | \$ 1,632    |
| <b>Net Income Used For Diluted Earnings Per Common Share</b>   |                                     |             |
| Income before discontinued operations and cumulative effect of accounting change   | \$ 1,484                            | \$ 1,282    |
| After-tax minority interest expense related to exchangeable equity interest  |                                     | 8           |
| After-tax interest expense related to zero-coupon convertible notes  |                                     | 7           |
| Income before discontinued operations, extraordinary item and cumulative effect of accounting change after assumed conversion of dilutive securities | 1,484                               | 1,297       |
| Income from discontinued operations, net of tax  | 142                                 | 392         |
| Extraordinary item, net of tax   | (131)                               |             |
| Cumulative effect of accounting change, net of tax   |                                     | (42)        |
| Net income after assumed conversion of dilutive securities   | \$ 1,495                            | \$ 1,647    |
| <b>Basic Earnings Per Common Share<sup>(1)</sup></b>   |                                     |             |
| Weighted-average shares outstanding basic  | 2,909                               | 2,915       |
| Income before discontinued operations, extraordinary item and cumulative effect of accounting change   | \$ .51                              | \$ .44      |
| Income from discontinued operations, net of tax  | .05                                 | .13         |
| Extraordinary item, net of tax   | (.05)                               |             |
| Cumulative effect of accounting change, net of tax   |                                     | (.01)       |
| Net income   | \$ .51                              | \$ .56      |
| <b>Diluted Earnings Per Common Share<sup>(1)</sup></b>   |                                     |             |
| Weighted-average shares outstanding  | 2,909                               | 2,915       |
| Effect of dilutive securities:   |                                     |             |
| Stock options  | 2                                   | 1           |
| Exchangeable equity interest   |                                     | 30          |
| Zero-coupon convertible notes  |                                     | 17          |
| Weighted-average shares diluted  | 2,911                               | 2,963       |
| Income before discontinued operations, extraordinary item and cumulative effect of accounting change   | \$ .51                              | \$ .44      |
| Income from discontinued operations, net of tax  | .05                                 | .13         |
| Extraordinary item, net of tax   | (.05)                               |             |
| Cumulative effect of accounting change, net of tax   |                                     | (.01)       |

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|            |    |     |    |     |
|------------|----|-----|----|-----|
| Net income | \$ | .51 | \$ | .56 |
|------------|----|-----|----|-----|

<sup>(1)</sup> Total of per share amounts may not add due to rounding.

Certain outstanding options to purchase shares were not included in the computation of diluted earnings per common share because to do so would have been anti-dilutive for the period, including approximately 181 million shares and 236 million shares for the three months ended March 31, 2007 and 2006, respectively.

The zero-coupon convertible notes were retired on May 15, 2006. Additionally, the Price Communications Corp. exchangeable equity interest was converted on August 15, 2006 by issuing 29.5 million Verizon shares.

**Table of Contents****9. Stock-Based Compensation**

Effective January 1, 2006, we adopted SFAS No. 123(R), *Share-Based Payments*, utilizing the modified prospective method. The impact to Verizon primarily resulted from Verizon Wireless, for which we recorded a \$42 million cumulative effect of accounting change, net of taxes and after minority interest, to recognize the effect of initially measuring the outstanding liability for awards granted to Domestic Wireless employees at fair value utilizing a Black-Scholes model.

*Restricted Stock Units*

The Verizon Communications Long Term Incentive Plan (the Plan) provides for grants of restricted stock units (RSUs) that vest at the end of the third year after the grant. The RSUs are classified as liability awards because the RSUs will be paid in cash upon vesting.

The following table summarizes Verizon's Restricted Stock Unit activity:

| (Shares in Thousands)                                     | <b>Restricted<br/>Stock Units</b> | <b>Weighted-Average<br/>Grant-Date<br/>Fair Value</b> |
|---|-----------------------------------|---|
| Outstanding, beginning of year                            | 15,593                            | \$ 33.67  |
| Grants  | 5,959                             | 37.87   |
| Payments  | (602)                             | 36.75   |
| Cancellations/Forfeitures                                 | (20)                              | 33.29   |
| <b>Outstanding restricted stock units, March 31, 2007</b> | <b>20,930</b>                     | <b>34.78</b>  |

*Performance Share Units*

The Plan also provides for grants of performance share units (PSUs) that vest at the end of the third year after the grant. The PSUs are classified as liability awards because the PSUs will be paid in cash upon vesting.

The following table summarizes Verizon's Performance Share Unit activity:

| (Shares in Thousands)                                      | <b>Performance<br/>Share Units</b> | <b>Weighted-Average<br/>Grant-Date<br/>Fair Value</b> |
|--|------------------------------------|---|
| Outstanding, beginning of year                             | 28,423                             | \$ 34.22  |
| Grants   | 9,204                              | 37.87   |
| Payments   | (5,759)                            | 36.75   |
| Cancellations/Forfeitures                                  | (661)                              | 36.66   |
| <b>Outstanding performance share units, March 31, 2007</b> | <b>31,207</b>                      | <b>34.78</b>  |

As of March 31, 2007, unrecognized compensation expense related to the unvested portion of Verizon's RSUs and PSUs was approximately \$783 million and is expected to be recognized over a weighted-average period of approximately two years.

*Verizon Wireless Long-Term Incentive Plan*

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The 2000 Verizon Wireless Long-Term Incentive Plan (the Wireless Plan ) provides compensation opportunities to eligible employees and other participating affiliates of the Cellco Partnership, d.b.a. Verizon Wireless (the Partnership ). The Wireless Plan provides rewards that are tied to the long-term performance of the Partnership. Under the Wireless Plan, Value Appreciation Rights (VARs) are granted to eligible employees. With the adoption of SFAS 123(R), the Partnership began estimating the fair value of VARs granted using a Black-Scholes option valuation model. As of March 31, 2007, substantially all VARs were fully vested.

The following table summarizes the VARs activity:

| (Shares in Thousands)  | <b>VARs</b>   | <b>Weighted-Average<br/>Grant-Date<br/>Fair Value</b> |
|--|---------------|---|
| Outstanding, beginning of year                               | 94,467        | \$ 16.99  |
| Exercises  | (2,124)       | 14.18   |
| Cancellations/Forfeitures                                    | (953)         | 23.16   |
| <b>Outstanding value appreciation rights, March 31, 2007</b> | <b>91,390</b> | <b>16.99</b>  |

**Table of Contents***Stock-Based Compensation Expense*

After-tax compensation expense for stock-based compensation described above included in net income as reported for the three months ended March 31, 2007 and 2006 was \$202 million and \$102 million, respectively.

*Stock Options*

The Verizon Long Term Incentive Plan provides for grants of stock options to employees at an option price per share of 100% of the fair market value of Verizon stock on the date of grant. Each grant has a 10 year life, vesting equally over a three year period, starting at the date of the grant. We have not granted new stock options since 2004. We determined stock-option related employee compensation expense for the 2004 grant using the Black-Scholes option-pricing model.

The following table summarizes Verizon's stock option activity:

| (Shares in Thousands)                      | <b>Stock Options</b> | <b>Weighted-Average<br/>Exercise Price</b> |
|--|----------------------|--|
| Options outstanding, beginning of year     | 229,364              | \$ 46.48                                   |
| Exercises                                  | (3,019)              | 35.61                                      |
| Cancellations                              | (10,419)             | 47.06                                      |
| <b>Options outstanding, March 31, 2007</b> | <b>215,926</b>       | <b>46.61</b>                               |
| <b>Options exercisable, March 31, 2007</b> | <b>215,909</b>       | <b>46.61</b>                               |

The weighted-average remaining contractual term was 3.6 years for stock options outstanding and exercisable as of March 31, 2007. The total intrinsic value was approximately \$65 million for stock options outstanding and exercisable as of March 31, 2007. For the three months ended March 31, 2007 and 2006, the amount of cash received from the exercise of stock options was approximately \$113 million and \$6 million, respectively. The total intrinsic value for stock options exercised during the first quarter of 2007 and 2006 and the related tax benefits were not material.

For the three months ended March 31, 2007 and 2006, after-tax compensation expense for stock options was \$2 million and \$10 million, respectively.

**10. Employee Benefits**

We maintain noncontributory defined benefit pension plans for many of our employees. In addition, we maintain postretirement health care and life insurance plans for our retirees and their dependents, which are both contributory and non-contributory and include a limit on the company's share of cost for certain recent and future retirees.

*Net Periodic Benefit (Income) Cost*

The following table summarizes the benefit costs (income) related to our pension and postretirement health care and life insurance plans:

(Dollars in Millions)

| <b>Three Months Ended March 31,</b> | <b>Pension</b> |             | <b>Health Care and Life</b> |             |
|-------------------------------------|----------------|-------------|-----------------------------|-------------|
|                                     | <b>2007</b>    | <b>2006</b> | <b>2007</b>                 | <b>2006</b> |
| Service cost                        | \$ 111         | \$ 176      | \$ 88                       | \$ 89       |
| Interest cost                       | 494            | 499         | 398                         | 374         |
| Expected return on plan assets      | (794)          | (793)       | (79)                        | (82)        |

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|                                    |          |         |        |        |
|------------------------------------|----------|---------|--------|--------|
| Amortization of prior service cost | 11       | 11      | 98     | 89     |
| Actuarial loss, net                | 24       | 45      | 79     | 73     |
| Net periodic benefit (income) cost | \$ (154) | \$ (62) | \$ 584 | \$ 543 |

**Table of Contents****Employer Contributions**

During the three months ended March 31, 2007, we contributed \$489 million to our qualified pension trusts, \$60 million to our nonqualified pension plans and \$293 million to our other postretirement benefit plans. Our estimate of the amount and timing of required qualified pension trust contributions for 2007 is based on current regulations, including continued pension funding relief. The anticipated required qualified pension trust contributions disclosed in Verizon's Annual Report on Form 10-K for the year ended December 31, 2006 continue to be accurate.

*Severance Benefits*

During the three months ended March 31, 2007, we paid severance benefits of \$98 million excluding amounts related to the MCI acquisition (see Note 4). At March 31, 2007, we had a remaining severance liability of \$557 million, which includes future contractual payments to employees separated as of March 31, 2007.

**11. Comprehensive Income**

Comprehensive income consists of net income and other gains and losses affecting shareowners' investment that, under accounting principles generally accepted in the United States, are excluded from net income.

Changes in the components of other comprehensive income were as follows:

| (Dollars in Millions)                                  | <b>Three Months Ended March 31,</b> |             |
|--|-------------------------------------|-------------|
|  | <b>2007</b>                         | <b>2006</b> |
| <b>Net Income</b>                                      | \$ 1,495                            | \$ 1,632    |
| <b>Other Comprehensive Income (Loss), Net of Taxes</b> |                                     |             |
| Foreign currency translation adjustments               | 17                                  | 79          |
| Unrealized derivative gains on cash flow hedges        | 6                                   | 12          |
| Unrealized (loss) gains on marketable securities       | (6)                                 | 24          |
| Minimum pension liability adjustment                   |                                     | 13          |
| Defined benefit pension and postretirement plans       | 136                                 |             |
| Disposition of TELPRI and other                        | 241                                 |             |
|  | 394                                 | 128         |
| <b>Total Comprehensive Income</b>                      | \$ 1,889                            | \$ 1,760    |

The unrealized foreign currency translation gain in the first quarter of 2006 is primarily driven by the appreciation in the functional currencies on our investments in Vodafone Omnitel N.V. (Vodafone Omnitel) and Verizon Dominicana, C. por A. (Verizon Dominicana).

The components of accumulated other comprehensive loss were as follows:

| (Dollars in Millions)                            | <b>At March 31, 2007</b> | <b>At December 31, 2006</b> |
|--|--------------------------|-----------------------------|
| Foreign currency translation adjustments         | \$ 346                   | \$ 329                      |
| Net unrealized losses on hedging                 | (5)                      | (11)                        |
| Unrealized gains on marketable securities        | 58                       | 64                          |
| Defined benefit pension and postretirement plans | (7,535)                  | (7,671)                     |
| Other  |                          | (241)                       |
| <b>Accumulated Other Comprehensive Loss</b>      | \$ (7,136)               | \$ (7,530)                  |





**Table of Contents****12. Segment Information**

We have two reportable segments, which we operate and manage as strategic business units and organize by products and services. Our segments are Wireline and Domestic Wireless. We measure and evaluate our reportable segments based on segment income. Corporate, eliminations and other includes unallocated corporate expenses, intersegment eliminations recorded in consolidation, the results of other businesses such as our investments in unconsolidated businesses, primarily Vodafone Omnitel, lease financing, and asset impairments and expenses that are not allocated in assessing segment performance due to their non-recurring nature. These adjustments include transactions that the chief operating decision makers exclude in assessing business unit performance due primarily to their non-recurring and/or non-operational nature. Although such transactions are excluded from the business segment results, they are included in reported consolidated earnings. Gains and losses that are not individually significant are included in all segment results, since these items are included in the chief operating decision makers' assessment of unit performance.

Our segments and their principal activities consist of the following:

| Segment                  | Description   |
|--------------------------|---|
| <b>Wireline</b>          | Wireline provides communications services including voice, broadband video and data, next generation IP network services, network access, long distance and other services to consumers, carriers, business and government customers both domestically and globally in 150 countries. |
| <b>Domestic Wireless</b> | Domestic Wireless' products and services include wireless voice and data products and other value added services and equipment sales across the United States.  |

The following table provides operating financial information for our two reportable segments:

| (Dollars in Millions)              | Three Months Ended March 31, |           |
|------------------------------------|------------------------------|-----------|
|                                    | 2007                         | 2006      |
| <b>External Operating Revenues</b> |                              |           |
| Wireline                           | \$ 12,166                    | \$ 12,214 |
| Domestic Wireless                  | 10,282                       | 8,796     |
| Total segments                     | 22,448                       | 21,010    |
| Reconciling items                  | 136                          | 221       |
| Total consolidated reported        | \$ 22,584                    | \$ 21,231 |
| <b>Intersegment Revenues</b>       |                              |           |
| Wireline                           | \$ 310                       | \$ 251    |
| Domestic Wireless                  | 25                           | 17        |
| Total segments                     | 335                          | 268       |
| Reconciling items                  | (335)                        | (268)     |
| Total consolidated reported        | \$                           | \$        |
| <b>Total Operating Revenues</b>    |                              |           |
| Wireline                           | \$ 12,476                    | \$ 12,465 |
| Domestic Wireless                  | 10,307                       | 8,813     |

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|                         |          |           |    |        |
|-------------------------|----------|-----------|----|--------|
| Total segments          |          | 22,783    |    | 21,278 |
| Reconciling items       |          | (199)     |    | (47)   |
| Total consolidated      | reported | \$ 22,584 | \$ | 21,231 |
| <b>Operating Income</b> |          |           |    |        |
| Wireline                |          | \$ 1,135  | \$ | 1,076  |
| Domestic Wireless       |          | 2,729     |    | 2,115  |
| Total segments          |          | 3,864     |    | 3,191  |
| Reconciling items       |          | (68)      |    | (16)   |
| Total consolidated      | reported | \$ 3,796  | \$ | 3,175  |

**Table of Contents**

| (Dollars in Millions)       | Three Months Ended March 31, |                             |
|-----------------------------|------------------------------|-----------------------------|
|                             | 2007                         | 2006                        |
| <b>Segment Income</b>       |                              |                             |
| Wireline                    | \$ 365                       | \$ 318                      |
| Domestic Wireless           | 874                          | 631                         |
| Total segment income        | 1,239                        | 949                         |
| Reconciling items           | 256                          | 683                         |
| Total consolidated reported | \$ 1,495                     | \$ 1,632                    |
|                             | <b>At March 31, 2007</b>     | <b>At December 31, 2006</b> |
| <b>Assets</b>               |                              |                             |
| Wireline                    | \$ 90,467                    | \$ 92,274                   |
| Domestic Wireless           | 82,078                       | 81,989                      |
| Total segments              | 172,545                      | 174,263                     |
| Reconciling items           | 11,739                       | 14,541                      |
| Total consolidated reported | \$ 184,284                   | \$ 188,804                  |

Major reconciling items between the segments and the consolidated results were as follows:

| (Dollars in Millions)                               | Three Months Ended March 31, |         |
|---|------------------------------|---------|
|   | 2007                         | 2006    |
| <b>Operating Revenues</b>                           |                              |         |
| Corporate, eliminations and other                   | \$ (199)                     | \$ (47) |
|   | \$ (199)                     | \$ (47) |
| <b>Operating Income</b>                             |                              |         |
| Verizon Center relocation, net (see Note 5)         | \$                           | \$ (46) |
| Merger integration costs (see Note 4)               | (14)                         | (55)    |
| Verizon Foundation contribution (see Note 2)        | (100)                        |         |
| Corporate and other                                 | 46                           | 85      |
|   | \$ (68)                      | \$ (16) |
| <b>Net Income</b>                                   |                              |         |
| Debt extinguishment costs (see Note 7)              | \$                           | \$ (16) |
| Verizon Center relocation, net (see Note 5)         |                              | (28)    |
| Merger integration costs (see Note 4)               | (9)                          | (35)    |
| Cumulative effect of accounting change (see Note 9) |                              | (42)    |
| Verizon Foundation contribution (see Note 2)        | (65)                         |         |
| Sale of Puerto Rico, net (see Note 2)               | 70                           |         |
| Extraordinary item, net of tax (see Note 2)         | (131)                        |         |
| Corporate and other                                 | 391                          | 804     |

We generally account for intersegment sales of products and services and asset transfers at current market prices. We are not dependent on any single customer.

**Table of Contents****13. Guarantees of Operating Subsidiary Debt**

Verizon has guaranteed \$480 million 7% debentures series B, due 2042 issued by Verizon New England Inc., a wholly-owned operating subsidiary. This guarantee would require Verizon to make scheduled payments immediately if the subsidiary failed to do so. The debentures were issued in denominations of \$25 and were sold primarily to retail investors and are listed on the New York Stock Exchange. SEC rules permit us to include condensed consolidating financial information for this subsidiary in our periodic SEC reports rather than filing separate subsidiary periodic SEC reports.

On March 23, 2007, Verizon redeemed the previously guaranteed \$300 million 7% debentures series F issued by Verizon South Inc. due 2041. Accordingly, we are no longer required to disclose this financial information in the condensed consolidating financial information.

Below is the condensed consolidating financial information. Verizon New England is presented in a separate column. The column labeled Parent represents Verizon's investments in all of its subsidiaries under the equity method and the Other column represents all other subsidiaries of Verizon on a combined basis. The Adjustments column reflects intercompany eliminations.

**Condensed Consolidating Statements of Income****Three Months Ended March 31, 2007**

| (Dollars in Millions)   | Parent   | Verizon New<br>England | Other     | Adjustments | Total     |
|---|----------|------------------------|-----------|-------------|-----------|
| Operating revenues  | \$       | \$ 923                 | \$ 21,827 | \$ (166)    | \$ 22,584 |
| Operating expenses  | 72       | 874                    | 18,008    | (166)       | 18,788    |
| <b>Operating income (loss)</b>  | (72)     | 49                     | 3,819     |             | 3,796     |
| Equity in earnings of unconsolidated businesses   | 1,431    |                        | (276)     | (995)       | 160       |
| Other income and (expense), net   | 444      | 6                      | 41        | (443)       | 48        |
| Interest expense  | (267)    | (45)                   | (180)     | 7           | (485)     |
| Minority interest   |          |                        | (1,154)   |             | (1,154)   |
| <b>Income before provision for income taxes, discontinued operations and extraordinary item</b> | 1,536    | 10                     | 2,250     | (1,431)     | 2,365     |
| Provision for income taxes  | (41)     | (2)                    | (838)     |             | (881)     |
| <b>Income before discontinued operations and extraordinary item</b>                             | 1,495    | 8                      | 1,412     | (1,431)     | 1,484     |
| Income from discontinued operations, net of tax   |          |                        | 142       |             | 142       |
| Extraordinary item, net of tax  |          |                        | (131)     |             | (131)     |
| <b>Net income</b>   | \$ 1,495 | \$ 8                   | \$ 1,423  | \$ (1,431)  | \$ 1,495  |

**Table of Contents****Condensed Consolidating Statements of Income****Three Months Ended March 31, 2006**

| (Dollars in Millions)   | Parent   | Verizon New<br>England | Other     | Adjustments | Total     |
|---|----------|------------------------|-----------|-------------|-----------|
| Operating revenues  | \$       | \$ 938                 | \$ 20,447 | \$ (154)    | \$ 21,231 |
| Operating expenses  | 5        | 874                    | 17,331    | (154)       | 18,056    |
| <b>Operating income (loss)</b>  | (5)      | 64                     | 3,116     |             | 3,175     |
| Equity in earnings of unconsolidated businesses   | 1,554    | 3                      | (117)     | (1,283)     | 157       |
| Other income and (expense), net   | 296      | 2                      | 83        | (278)       | 103       |
| Interest expense  | (204)    | (44)                   | (395)     | 7           | (636)     |
| Minority interest   |          |                        | (866)     |             | (866)     |
| <b>Income before provision for income taxes, discontinued operations and cumulative effect of accounting change</b> | 1,641    | 25                     | 1,821     | (1,554)     | 1,933     |
| Provision for income taxes  | (9)      | (7)                    | (635)     |             | (651)     |
| <b>Income before discontinued operations and cumulative effect of accounting change</b>                             | 1,632    | 18                     | 1,186     | (1,554)     | 1,282     |
| Income from discontinued operations, net of tax   |          |                        | 392       |             | 392       |
| Cumulative effect of accounting change, net of tax  |          |                        | (42)      |             | (42)      |
| <b>Net income</b>   | \$ 1,632 | \$ 18                  | \$ 1,536  | \$ (1,554)  | \$ 1,632  |

**Condensed Consolidating Balance Sheets****At March 31, 2007**

| (Dollars in Millions)                    | Parent    | Verizon New<br>England | Other      | Adjustments | Total      |
|--|-----------|------------------------|------------|-------------|------------|
| Cash                                     | \$        | \$                     | \$ 1,301   | \$          | \$ 1,301   |
| Short-term investments                   |           | 191                    | 1,958      |             | 2,149      |
| Accounts receivable, net                 | 3         | 649                    | 10,409     | (884)       | 10,177     |
| Other current assets                     | 30,211    | 183                    | 4,081      | (30,208)    | 4,267      |
| <b>Total current assets</b>              | 30,214    | 1,023                  | 17,749     | (31,092)    | 17,894     |
| Plant, property and equipment, net       | 1         | 6,145                  | 76,832     |             | 82,978     |
| Investments in unconsolidated businesses | 46,039    | 116                    | 6,184      | (47,441)    | 4,898      |
| Other assets                             | 4,946     | 300                    | 73,498     | (230)       | 78,514     |
| <b>Total assets</b>                      | \$ 81,200 | \$ 7,584               | \$ 174,263 | \$ (78,763) | \$ 184,284 |
| Debt maturing within one year            | \$ 5,922  | \$ 427                 | \$ 30,761  | \$ (30,506) | \$ 6,604   |
| Other current liabilities                | 2,208     | 940                    | 18,740     | (586)       | 21,302     |
| <b>Total current liabilities</b>         | 8,130     | 1,367                  | 49,501     | (31,092)    | 27,906     |
| Long-term debt                           | 11,754    | 2,574                  | 13,975     | (230)       | 28,073     |

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|   |                  |                 |                   |                    |                   |
|---|------------------|-----------------|-------------------|--------------------|-------------------|
| Employee benefit obligations                        | 12,223           | 1,595           | 15,925            |                    | 29,743            |
| Deferred income taxes                               | 65               | 455             | 12,998            |                    | 13,518            |
| Other liabilities                                   | 246              | 252             | 6,527             |                    | 7,025             |
| Minority interest                                   |                  |                 | 29,237            |                    | 29,237            |
| Total shareowners investment                        | 48,782           | 1,341           | 46,100            | (47,441)           | 48,782            |
| <b>Total liabilities and shareowners investment</b> | <b>\$ 81,200</b> | <b>\$ 7,584</b> | <b>\$ 174,263</b> | <b>\$ (78,763)</b> | <b>\$ 184,284</b> |

**Table of Contents****Condensed Consolidating Balance Sheets****At December 31, 2006**

| (Dollars in Millions)                               | Parent           | Verizon New<br>England | Other             | Adjustments        | Total             |
|---|------------------|------------------------|-------------------|--------------------|-------------------|
| Cash  | \$               | \$                     | \$ 3,219          | \$                 | \$ 3,219          |
| Short-term investments                              |                  | 215                    | 2,219             |                    | 2,434             |
| Accounts receivable, net                            | 4                | 705                    | 11,037            | (855)              | 10,891            |
| Other current assets                                | 32,680           | 134                    | 5,858             | (32,678)           | 5,994             |
| <b>Total current assets</b>                         | <b>32,684</b>    | <b>1,054</b>           | <b>22,333</b>     | <b>(33,533)</b>    | <b>22,538</b>     |
| Plant, property and equipment, net                  | 1                | 6,165                  | 76,190            |                    | 82,356            |
| Investments in unconsolidated businesses            | 44,048           | 116                    | 7,850             | (47,146)           | 4,868             |
| Other assets  | 5,045            | 288                    | 73,939            | (230)              | 79,042            |
| <b>Total assets</b>                                 | <b>\$ 81,778</b> | <b>\$ 7,623</b>        | <b>\$ 180,312</b> | <b>\$ (80,909)</b> | <b>\$ 188,804</b> |
| Debt maturing within one year                       | \$ 6,735         | \$ 333                 | \$ 33,527         | \$ (32,880)        | \$ 7,715          |
| Other current liabilities                           | 2,354            | 1,060                  | 21,804            | (653)              | 24,565            |
| <b>Total current liabilities</b>                    | <b>9,089</b>     | <b>1,393</b>           | <b>55,331</b>     | <b>(33,533)</b>    | <b>32,280</b>     |
| Long-term debt                                      | 11,392           | 2,573                  | 14,911            | (230)              | 28,646            |
| Employee benefit obligations                        | 12,419           | 1,625                  | 16,735            |                    | 30,779            |
| Deferred income taxes                               | 337              | 532                    | 15,401            |                    | 16,270            |
| Other liabilities                                   | 6                | 111                    | 3,840             |                    | 3,957             |
| Minority interest                                   |                  |                        | 28,337            |                    | 28,337            |
| Total shareowners investment                        | 48,535           | 1,389                  | 45,757            | (47,146)           | 48,535            |
| <b>Total liabilities and shareowners investment</b> | <b>\$ 81,778</b> | <b>\$ 7,623</b>        | <b>\$ 180,312</b> | <b>\$ (80,909)</b> | <b>\$ 188,804</b> |

**Condensed Consolidating Statements of Cash Flows****Three Months Ended March 31, 2007**

| (Dollars in Millions)              | Parent    | Verizon New<br>England | Other             | Adjustments | Total             |
|------------------------------------|-----------|------------------------|-------------------|-------------|-------------------|
| Net cash from operating activities | \$ 768    | \$ 129                 | \$ 4,404          | \$ (784)    | \$ 4,517          |
| Net cash from investing activities |           | (167)                  | (2,926)           | (94)        | (3,187)           |
| Net cash from financing activities | (768)     | 38                     | (3,396)           | 878         | (3,248)           |
| <b>Net decrease in cash</b>        | <b>\$</b> | <b>\$</b>              | <b>\$ (1,918)</b> | <b>\$</b>   | <b>\$ (1,918)</b> |

**Condensed Consolidating Statements of Cash Flows****Three Months Ended March 31, 2006**

| (Dollars in Millions)              | Parent | Verizon New<br>England | Other    | Adjustments | Total    |
|------------------------------------|--------|------------------------|----------|-------------|----------|
| Net cash from operating activities | \$ 748 | \$ 433                 | \$ 5,654 | \$ (769)    | \$ 6,066 |
| Net cash from investing activities | (779)  | (224)                  | (555)    | (190)       | (1,748)  |
| Net cash from financing activities | 31     | (209)                  | (4,611)  | 959         | (3,830)  |



|                             |    |    |    |     |    |    |     |
|-----------------------------|----|----|----|-----|----|----|-----|
| <b>Net increase in cash</b> | \$ | \$ | \$ | 488 | \$ | \$ | 488 |
|-----------------------------|----|----|----|-----|----|----|-----|

17

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**Table of Contents**

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**14. Other Recent Accounting Pronouncements**

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In February 2007, the Financial Accounting Standards Board issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of SFAS 115* (SFAS No. 159), which allows for the option to measure financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of SFAS No. 159 on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurement* (SFAS No. 157). SFAS No. 157 expands disclosures about fair value measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and establishes a hierarchy that categorizes and prioritizes the sources to be used to estimate fair value. We are required to adopt SFAS No. 157 effective January 1, 2008 on a prospective basis. We are currently evaluating the impact this new standard will have on our future results of operations and financial position.

In June 2006, the Emerging Issues Task Force (EITF) reached a consensus on EITF No. 06-3, *How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement* (EITF No. 06-3). EITF No. 06-3 permits that such taxes may be presented on either a gross basis or a net basis as long as that presentation is used consistently. The adoption of EITF No. 06-3 on January 1, 2007 did not impact our condensed consolidated financial statements. We present the taxes within the scope of EITF No. 06-3 on a net basis.

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**15. Commitments and Contingencies**

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Several state and federal regulatory proceedings may require our telephone operations to pay penalties or to refund to customers a portion of the revenues collected in the current and prior periods. There are also various legal actions pending to which we are a party and claims which, if asserted, may lead to other legal actions. We have established reserves for specific liabilities in connection with regulatory and legal actions, including environmental matters, that we currently deem to be probable and estimable. We do not expect that the ultimate resolution of pending regulatory and legal matters in future periods, including the Hicksville matters described below, will have a material effect on our financial condition, but it could have a material effect on our results of operations.

During 2003, under a government-approved plan, remediation commenced at the site of a former Sylvania facility in Hicksville, New York that processed nuclear fuel rods in the 1950s and 1960s. Remediation beyond original expectations proved to be necessary and a reassessment of the anticipated remediation costs was conducted. A reassessment of costs related to remediation efforts at several other former facilities was also undertaken. In September 2005 the Army Corps of Engineers (ACE) accepted the Hicksville site into the Formerly Utilized Sites Remedial Action Program. This may result in the ACE performing some or all of the remediation effort for the Hicksville site with a corresponding decrease in costs to Verizon. To the extent that the ACE assumes responsibility for remedial work at the Hicksville site, an adjustment to a reserve previously established for the remediation may be made. Adjustments may also be made based upon actual conditions discovered during the remediation at any of the sites requiring remediation.

There are also litigation matters associated with the Hicksville site primarily involving personal injury claims in connection with alleged emissions arising from operations in the 1950s and 1960s at the Hicksville site. These matters are in various stages, and no trial date has been set.

In connection with the execution of agreements for the sales of businesses and investments, Verizon ordinarily provides representations and warranties to the purchasers pertaining to a variety of nonfinancial matters, such as ownership of the securities being sold, as well as financial losses.

Under the terms of an investment agreement, as of December 31, 2006, Vodafone has the right to require the purchase of up to \$10 billion worth of its interest in Verizon Wireless, during a 61-day period opening on June 10 and closing on August 9 in 2007, under its one remaining put window. Vodafone also may require that Verizon Wireless pay for up to \$7.5 billion of the required repurchase through the assumption or incurrence of debt. In the event Vodafone fully exercises its one remaining put right, we (instead of Verizon Wireless) have the right, exercisable at our sole discretion, to purchase up to \$2.5 billion of the \$10 billion Vodafone interest for cash or Verizon stock at our option.

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations****Overview**

Verizon Communications Inc. (Verizon) is one of the world's leading providers of communications services. Verizon's wireline business provides telephone services, including voice, broadband data and video services, network access, nationwide long-distance and other communications products and services, and also owns and operates one of the most expansive end-to-end global Internet Protocol (IP) networks. Verizon's domestic wireless business, operating as Verizon Wireless, provides wireless voice and data products and services across the United States using one of the most extensive and reliable wireless networks. Stressing diversity and commitment to the communities in which we operate, Verizon has a highly diverse workforce of approximately 239,000 employees.

The sections that follow provide information about the important aspects of our operations and investments, both at the consolidated and segment levels, and include discussions of our results of operations, financial position and sources and uses of cash. In addition, we have highlighted key trends and uncertainties to the extent practicable. The content and organization of the financial and non-financial data presented in these sections are consistent with information used by our chief operating decision makers for, among other purposes, evaluating performance and allocating resources. We also monitor several key economic indicators as well as the state of the economy in general, primarily in the United States where the majority of our operations are located, in evaluating our operating results and analyzing and understanding business trends. While most key economic indicators, including gross domestic product, impact our operations to some degree, we have noted higher correlations to housing starts, non-farm employment, personal consumption expenditures and capital spending, as well as more general economic indicators such as inflation and unemployment rates.

Our results of operations, financial position and sources and uses of cash in the current and future periods reflect Verizon management's focus on the following four key areas:

**Revenue Growth** Our emphasis is on revenue growth, devoting more resources to higher growth markets such as wireless, including wireless data, wireline broadband connections, including fiber optics to the premises (Verizon's high-capacity fiber network (FiOS) and TV services), digital subscriber lines (DSL) and other data services, long distance, as well as expanded strategic services to business markets, rather than to the traditional wireline voice market, where we have been experiencing access line losses. During the first quarter of 2007, we reported consolidated revenue growth of 6.4% compared to last year, primarily driven by 17% higher revenue at Domestic Wireless, where we added approximately 1.7 million total wireless customers, of which over 1.6 million were wireless retail customers. Wireline remained stable as growth in enterprise business and broadband offset declines in wholesale and access line losses. Verizon Telecom added 416,000 broadband connections during the quarter.

**Operational Efficiency** While focusing resources on growth, we are continually challenging our management team to lower expenses, particularly through technology-assisted productivity improvements including self-service initiatives. The effect of these and other efforts, such as real estate consolidations, call center routing improvements and the formation of Verizon Services Organization, has been to change the company's cost structure and maintain stable operating income margins. Real estate consolidations include the establishment of the Verizon Center. The Verizon Services Organization provides centralized services across our business, including procurement, finance operations and real estate services. With our deployment of the FiOS network, we expect to realize savings in annual, ongoing operating expenses as a result of efficiencies gained from fiber network facilities. As the deployment of the FiOS network gains scale and installation automation improvements occur, costs per home connected are expected to decline. Since the merger with MCI, we have gained operational benefits from sales force and product and systems integration initiatives. Workforce levels in the first quarter of 2007 increased to 239,000 from 236,000, primarily from an increase in headcount at Domestic Wireless, partially offset by headcount reductions of about 8,000 in our wireline business, as a result of continued productivity improvements and merger synergy savings.

**Capital Allocation** Our capital spending continues to be directed toward growth markets. High-speed wireless data (Evolution-Data Optimized, or EV-DO) services, replacement of copper access lines with fiber optics to the premises, as well as expanded services to business markets are examples of areas of capital spending in support of these growth markets. Excluding discontinued operations, during the first quarter of 2007, capital expenditures were \$4,163 million compared to capital expenditures of \$4,021 million in the similar period in 2006. Of the increase, \$140 million was attributable to the growth initiatives at Domestic Wireless. In 2007, Verizon management expects capital expenditures to be in the range of \$17.5 billion to \$17.9 billion. In addition to capital expenditures, Verizon Wireless continues to

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participate in the Federal Communications Commission's (FCC) wireless spectrum auctions and continues to evaluate spectrum acquisitions in support of expanding data applications and its growing customer base.

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**Table of Contents**

**Cash Flow Generation and Shareowner Value Creation** The financial statements reflect the emphasis of management on not only directing resources to growth markets, but also creating value for shareowners through the use of cash provided by our operating and investing activities for the repayment of debt, share repurchases and providing a stable dividend to our shareowners, in addition to returning value to shareowners through spin-off and other strategic transactions. Verizon's total debt decreased by \$1,684 million to \$34,677 million as of March 31, 2007 from December 31, 2006, primarily as a result of debt repayments from the utilization of proceeds generated through strategic asset dispositions during 2006 and the first quarter of 2007. Verizon's ratio of debt to debt combined with shareowners' equity was 41.5% as of March 31, 2007 compared with 42.8% as of December 31, 2006. During the first quarter of 2007, we repurchased \$427 million of our common stock as part of our previously announced program, and we plan to continue our share buyback program at similar levels to 2006 during 2007. Verizon's balance of cash and cash equivalents at March 31, 2007 of \$1,301 million decreased by \$1,918 million from \$3,219 million at December 31, 2006.

Supporting these key focus areas are continuing initiatives to enhance the value of our products and services through well-managed deployment of proven advanced technology and through competitive products and services packaging. At Wireline, as of March 31, 2007, we passed 6.8 million premises with our high-capacity fiber network. We added 177,000 new FiOS data connections in the first quarter of 2007. In 2005, we began offering video on the FiOS network in three markets. By the end of the first quarter of 2007, Verizon had obtained over 760 video franchises covering 10.1 million households with service available for sale to 3.1 million premises. We had 348,000 FiOS TV customers by the end of the first quarter of 2007. We are also developing and marketing innovative product bundles to include local wireline, long distance, wireless and broadband services for consumer and general business retail customers. These efforts will also help counter the effects of competition and technology substitution that have resulted in access line losses, and will enable us to grow revenues by becoming a leading video provider.

Also at Wireline, we will continue to focus investments in strategic areas by rolling-out next generation global IP networks to meet the ongoing global enterprise market shift to IP-based products and services. Deployment of new strategic service offerings, including expansion of our voice over IP (VoIP) and international Ethernet capabilities, introduction of cutting edge video and web-based conferencing capabilities and enhancements to our virtual private network portfolio, will allow us to continue to gain share in the enterprise market. Additionally, we will continue to integrate the business of the former MCI to drive continued growth in synergy, supporting a focus on operational efficiency and continued creation of shareowner value.

At Verizon Wireless, we will continue to execute on the fundamentals of our network superiority and value proposition to deliver growth for the business and provide new and innovative products and services for our customers such as Broadband Access, our EV-DO service. To accomplish our goal of being the acknowledged market leader in providing wireless voice and data communication services in the U.S., we will continue to implement the following key elements of our business strategy: provide the highest network reliability through our code division multiple access (CDMA) 1XRTT technology and EV-DO (Revision A) infrastructure, which significantly increases data transmission rates; profitably acquire, satisfy and retain our customers; and increase the value of our service offerings to customers while achieving revenue and net income growth. We also continue to expand our wireless data, messaging and multi-media offerings for both consumer and business customers and take advantage of the growing demand for wireless data services and focus on operating margins and capital efficiency by driving down costs and leveraging our scale.

In January 2007, Verizon announced a definitive agreement with FairPoint Communications, Inc. (FairPoint) that will result in Verizon establishing a separate entity for its local exchange access lines and related business assets in Maine, New Hampshire and Vermont, spinning off that new entity to Verizon's shareowners, and immediately merging it with and into FairPoint. The total value to be received by Verizon and its shareowners in exchange for these operations will be approximately \$2,715 million. We expect this transaction to close within one year of the date of announcement.

**Table of Contents****Consolidated Results of Operations**

We have two reportable segments, which we operate and manage as strategic business units and organize by products and services. Our segments are Wireline and Domestic Wireless. Prior period amounts and discussions are revised to reflect this change. We include in our results of operations the results of the former MCI business subsequent to the close of the merger on January 6, 2006.

This section on consolidated results of operations carries forward the segment results, which exclude the special and non-recurring items, and highlights and describes those items separately to ensure consistency of presentation in this section and the Segment Results of Operations section. In the following section, we review the performance of our two reportable segments. We exclude the effects of the special and non-recurring items from the segments' results of operations since management does not consider them in assessing segment performance, due primarily to their non-recurring and/or non-operational nature. We believe that this presentation will assist readers in better understanding our results of operations and trends from period to period.

**Consolidated Revenues**

| (Dollars in Millions)        | Three Months Ended March 31, |           |          |
|------------------------------|------------------------------|-----------|----------|
|                              | 2007                         | 2006      | % Change |
| <b>Wireline</b>              |                              |           |          |
| Verizon Telecom              | \$ 7,984                     | \$ 8,265  | (3.4)    |
| Verizon Business             | 5,219                        | 4,924     | 6.0      |
| Intrasegment eliminations    | (727)                        | (724)     | 0.4      |
|                              | 12,476                       | 12,465    | 0.1      |
| <b>Domestic Wireless</b>     | 10,307                       | 8,813     | 17.0     |
| Corporate & Other            | (199)                        | (47)      | nm       |
| <b>Consolidated Revenues</b> | \$ 22,584                    | \$ 21,231 | 6.4      |

nm Not meaningful

Consolidated revenues in the first quarter of 2007 were higher by \$1,353 million, or 6.4% compared to the similar period in 2006. This increase was primarily the result of continued strong growth at Domestic Wireless.

Wireline's revenues during the first quarter of 2007 increased by \$11 million, or 0.1% compared to last year, partly due to a full quarter of results for the former MCI operations and growth from broadband and long distance services. We added 416,000 new broadband connections, including 177,000 for FiOS, in the first quarter of 2007, for a total of 7,398,000 lines at March 31, 2007, representing a 30.1% increase from March 31, 2006. In addition, we added 141,000 FiOS TV customers in the first quarter of 2007, for a total of 348,000 at March 31, 2007. These increases were partially offset by a decline in voice revenues at Verizon Telecom due to subscriber losses resulting from technology substitution, including wireless and VoIP. Revenues at Verizon Business increased primarily due to the acquisition of MCI and the higher demand for Internet related product offerings.

**Table of Contents**

Domestic Wireless revenues increased by \$1,494 million, or 17.0% compared to the similar period in 2006 due to increases in service revenues, including data revenues, and equipment and other revenues. Data revenues increased by \$697 million or 80% compared to the similar period last year. Domestic Wireless customers at March 31, 2007 were approximately 61 million, an increase of 14.5% over last year. Domestic Wireless retail customer base as of March 31, 2007 was approximately 58 million, a 15.4% increase from March 31, 2006, and comprised approximately 96.3% of our total customer base. Average service revenue per customer (ARPU) increased by 2.9% to \$50.06 in the first quarter of 2007 compared to 2006, primarily attributable to increases in data revenue per customer driven by increased use of our messaging and other data services. Retail ARPU increased by 2.8% to \$50.73 for the first quarter of 2007 compared to 2006. Increases in wireless devices sold and revenue per unit sold drove increases in equipment and other revenue during the first quarter of 2007 compared to 2006.

**Consolidated Operating Expenses**

| (Dollars in Millions)                       | Three Months Ended March 31, |                  |            |
|---|------------------------------|------------------|------------|
|   | 2007                         | 2006             | % Change   |
| Cost of services and sales                  | \$ 8,912                     | \$ 8,516         | 4.7        |
| Selling, general and administrative expense | 6,343                        | 5,873            | 8.0        |
| Depreciation and amortization expense       | 3,533                        | 3,667            | (3.7)      |
| <b>Consolidated Operating Expenses</b>      | <b>\$ 18,788</b>             | <b>\$ 18,056</b> | <b>4.1</b> |

*Cost of Services and Sales*

Consolidated cost of services and sales in first quarter 2007 increased \$396 million, or 4.7% compared to the similar period in 2006 primarily as a result of higher wireless network costs and increases in wireless equipment costs, partially offset by decreases in pension and other postretirement benefit costs and the impact of productivity improvement initiatives.

The higher wireless network costs were caused by increased network usage relating to both voice and data services in the first quarter of 2007 compared to the similar period in 2006, partially offset by decreased local interconnection, long distance and roaming rates. Cost of wireless equipment sales increased in the first quarter of 2007 compared to the similar period in 2006 primarily as a result of an increase in wireless devices sold due to an increase in gross retail activations and equipment upgrades in the first quarter of 2007 compared to the similar period in 2006. Costs in this period were also impacted by decreased net pension and other postretirement benefit costs. As of December 31, 2006, we evaluated key employee benefit plan assumptions in response to current conditions in the securities markets. The overall impact of the 2007 assumptions, combined with the impact of the management pension freeze, effective June 30, 2006, resulted in pension and other postretirement benefit expense of \$323 million (primarily in cost of services and sales) in the first quarter of 2007 compared to \$370 million in the first quarter of 2006.

*Selling, General and Administrative Expense*

Consolidated selling, general and administrative expense in first quarter 2007 increased by \$470 million, or 8% compared to the similar period in 2006. This increase was primarily attributable to higher salary and benefits expense, primarily driven by an increase in costs related to the employees long-term incentive program and an increase in employees at Domestic Wireless, as well as higher sales commission expense as a result of a strong increase in customer additions, renewals and upgrades. Partially offsetting the increase were lower bad debt expenses and other cost reduction initiatives across all segments.

Special and non-recurring items in the first quarter of 2007 included \$14 million of merger integration costs, primarily comprised of Wireline systems integration activities and a \$100 million contribution to Verizon Foundation, as a result of the sale of TELPRI, to fund its charitable activities and increase its self-sufficiency.

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Special and non-recurring items in the first quarter of 2006 included \$55 million of continued merger integration costs and other costs related to re-branding initiatives and \$46 million related to Verizon Center relocation costs.



**Table of Contents****Depreciation and Amortization Expense**

Depreciation and amortization expense decreased by \$134 million, or 3.7% in the first quarter of 2007 compared to the similar period last year. This decrease was primarily due to lower rates of depreciation as a result of changes in the estimated useful lives of certain asset classes and fully amortized customer lists, partially offset by growth in depreciable telephone plant and increased capital expenditures.

**Other Consolidated Results***Other Income and (Expense), Net*

| (Dollars in Millions)       | Three Months Ended March 31, |        | % Change |
|-----------------------------|------------------------------|--------|----------|
|                             | 2007                         | 2006   |          |
| Interest income             | \$ 44                        | \$ 55  | (20.0)   |
| Foreign exchange gains, net | 8                            | 10     | (20.0)   |
| Other, net                  | (4)                          | 38     | nm       |
| Total                       | \$ 48                        | \$ 103 | (53.4)   |

nm Not meaningful

Other Income and (Expense), Net for the first quarter of 2007 decreased \$55 million, or 53.4% compared to the similar period last year. The decline was primarily due to decreased interest income as a result of lower average cash balances.

*Interest Expense*

| (Dollars in Millions)                 | Three Months Ended March 31, |           | % Change |
|---------------------------------------|------------------------------|-----------|----------|
|                                       | 2007                         | 2006      |          |
| Interest expense                      | \$ 485                       | \$ 636    | (23.7)   |
| Capitalized interest costs            | 109                          | 108       | 0.9      |
| Total interest costs on debt balances | \$ 594                       | \$ 744    | (20.2)   |
| Weighted-average debt outstanding     | \$ 35,216                    | \$ 42,839 |          |
| Effective interest rate               | 6.7%                         | 7.0%      |          |

During the first quarter of 2007, total interest costs decreased \$150 million, compared to the similar period in 2006, primarily due to a decrease in the weighted-average debt level and lower interest rates compared to last year. The weighted-average debt level decreased primarily as a result of the approximately \$7.1 billion reduction from the spin-off of Idearc as well as from the proceeds from the sale of Verizon Dominicana in the fourth quarter of 2006.

*Minority Interest*

| (Dollars in Millions) | Three Months Ended March 31, |        | % Change |
|-----------------------|------------------------------|--------|----------|
|                       | 2007                         | 2006   |          |
| Minority interest     | \$ 1,154                     | \$ 866 | 33.3     |

The increase in minority interest expense in the first quarter of 2007 compared to similar periods in 2006 was primarily due to the higher earnings at Domestic Wireless, which has a significant minority interest attributable to Vodafone Group Plc (Vodafone).

**Table of Contents***Provision for Income Taxes*

| (Dollars in Millions)      | <b>Three Months Ended March 31,</b> |             |                 |
|----------------------------|-------------------------------------|-------------|-----------------|
|                            | <b>2007</b>                         | <b>2006</b> | <b>% Change</b> |
| Provision for income taxes | \$ 881                              | \$ 651      | 35.3            |
| Effective income tax rate  | 37.3%                               | 33.7%       |                 |

The effective income tax rate is the provision for income taxes as a percentage of income from continuing operations before the provision for income taxes. The effective tax rate for the first quarter of 2007 compared to the similar period of 2006 was higher due to the larger favorable tax reserve adjustments and income tax credits recorded in 2006. In addition, the 2007 effective tax rate was higher compared to 2006 as a result of a larger impact in 2007 of the Wireless minority interest as well as lower tax benefits from foreign operations in 2007 compared to 2006.

*Discontinued Operations*

On March 27, 2007, the Federal Communications Commission approved the sale of Telecomunicaciones de Puerto Rico, Inc. (TELPRI) to América Móvil, S.A.B. de C.V. (América Móvil). On March 30, 2007, we completed the previously announced sale of our interest in TELPRI to a subsidiary of América Móvil and recorded a pretax gain of \$120 million (\$70 million after-tax, or \$.02 per diluted share). América Móvil purchased 100% of TELPRI, the holding company of Puerto Rico Telephone Company, including Verizon's 52% interest. Accordingly, discontinued operations in the consolidated statements of income for the three months ended March 31, 2007 includes the results of operations of TELPRI through the completion of the sale.

Discontinued operations for the three months ended March 31, 2006 includes our former U.S. print and Internet yellow pages directories business and Verizon Dominicana in the condensed consolidated statements of income, both of which were disposed of during the fourth quarter of 2006.

*Extraordinary Item*

In January 2007, the Bolivarian Republic of Venezuela (the Republic) declared its intent to nationalize certain companies, including CANTV. On February 12, 2007, we entered into a Memorandum of Understanding (MOU) with the Republic. The MOU provides that the Republic will offer to purchase all of the equity securities of CANTV, including our 28.5% interest, through public tender offers in Venezuela and the United States at a price equivalent to \$17.85 per American Depository Share (ADS), subject to adjustment if CANTV declared and paid a dividend prior to the purchase of the equity securities in the tender offers. A dividend of 6,454.49 Bolívares per ADS (equivalent to \$3.00 at the current official exchange rate) with an April 18, 2007 payment date was recommended by the CANTV Board and then approved by shareholders on March 30, 2007. The Republic launched the public tender offers on April 9, 2007 at a price equivalent to \$14.85 per ADS. Unless extended, the offers will expire on May 8, 2007. The price is subject to further adjustment for any additional dividends declared and paid before the date the equity securities are accepted for payment, and in the event of a change in the official exchange rate, for changes to the equivalent dollar value of the April 18 dividend. The tender offers are subject to certain conditions including that a majority of the outstanding shares are tendered to the Republic. Based upon the terms of the MOU and our current investment balance in CANTV, we recorded an extraordinary loss on our investment of \$131 million, net of tax, or \$.05 per diluted share, in the first quarter of 2007. If the tender offers are completed, Verizon expects to receive an aggregate amount of \$572 million through a combination of purchase price and the 2007 dividend.

*Cumulative Effect of Accounting Change*

Effective January 1, 2006, we adopted SFAS No. 123(R), *Share-Based Payments*, utilizing the modified prospective method. The impact to Verizon primarily resulted from Verizon Wireless, for which we recorded a \$42 million cumulative effect of accounting change, net of taxes and after minority interest, to recognize the effect of initially measuring the outstanding liability for awards granted to Domestic Wireless employees at fair value utilizing a Black-Scholes model.

**Table of Contents****Segment Results of Operations**

We have two reportable segments, which we operate and manage as strategic business units and organize by products and services. Our segments are Wireline and Domestic Wireless. You can find additional information about our segments in Note 12 to the consolidated financial statements.

We measure and evaluate our reportable segments based on segment income. Corporate, eliminations and other includes unallocated corporate expenses, intersegment eliminations recorded in consolidation, the results of other businesses such as our investments in unconsolidated businesses, primarily Vodafone Omnitel N.V. (Vodafone Omnitel), lease financing, and asset impairments and expenses that are not allocated in assessing segment performance due to their non-recurring nature. These adjustments include transactions that the chief operating decision makers exclude in assessing business unit performance due primarily to their non-recurring and/or non-operational nature. Although such transactions are excluded from the business segment results, they are included in reported consolidated earnings. Gains and losses that are not individually significant are included in all segment results, since these items are included in the chief operating decision makers' assessment of unit performance.

**Wireline**

The Wireline segment consists of the operations of Verizon Telecom, a provider of communications services, including voice, broadband video and data, network access, long distance, and other services to consumer and small business customers and carriers, and Verizon Business, a provider of next-generation IP network services globally to medium and large businesses and government customers. Operating results shown for 2006 exclude the results of the former MCI prior to the date of the merger (January 6, 2006).

**Operating Revenues**

| (Dollars in Millions)             | Three Months Ended March 31, |           | % Change |
|-----------------------------------|------------------------------|-----------|----------|
|                                   | 2007                         | 2006      |          |
| Verizon Telecom                   |                              |           |          |
| Mass Markets                      | \$ 5,506                     | \$ 5,584  | (1.4)    |
| Wholesale                         | 1,997                        | 2,064     | (3.2)    |
| Other                             | 481                          | 617       | (22.0)   |
| Verizon Business                  |                              |           |          |
| Enterprise Business               | 3,571                        | 3,383     | 5.6      |
| Wholesale                         | 850                          | 804       | 5.7      |
| International and Other           | 798                          | 737       | 8.3      |
| Intrasegment Eliminations         | (727)                        | (724)     | 0.4      |
| Total Wireline Operating Revenues | \$ 12,476                    | \$ 12,465 | 0.1      |

*Verizon Telecom*

**Mass Markets**

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Verizon Telecom's Mass Markets revenue includes local exchange (basic service and end-user access), value-added services, long distance, broadband services for residential and certain small business accounts and FiOS TV services. Also included are revenues generated from former MCI consumer and business products and services. Value-added services are a family of services that expand the utilization of the network, including products such as Caller ID, Call Waiting, Home Voicemail and Return Call. Long distance includes both regional toll services and long distance services. Broadband services include DSL and FiOS.

The decrease in mass market revenue of \$78 million, or 1.4% in the first quarter of 2007 compared to the similar period in 2006 was due to lower demand and usage of our basic local exchange and accompanying services, attributable to subscriber losses, including losses of customers of former MCI, as a result of technology substitution, including wireless and Voice over Internet Protocol (VoIP). These decreases were partially offset by growth from broadband, long distance and the inclusion of the former MCI for the full quarter in 2007.

## Table of Contents

A 7.9% decline in switched access lines in service from March 31, 2006 was mainly driven by the effects of competition and technology substitution. Residential retail access lines declined 9.3% at March 31, 2007 compared to March 31, 2006, as customers substituted wireless, broadband and cable services for traditional landline services. At the same time, small business retail access lines declined 3.4% at March 31, 2007 compared to March 31, 2006, primarily reflecting competition and a shift to high-speed, high-volume special access lines. Access line losses include the loss of lines served by former MCI.

We added 416,000 new broadband connections, including 177,000 for FiOS data, in the first quarter of 2007, for a total of 7,398,000 lines at March 31, 2007, representing a 30.1% increase from March 31, 2006. In addition, we added 141,000 FiOS TV customers in the first quarter of 2007, for a total of 348,000 at March 31, 2007. As of March 31, 2007, for FiOS data and FiOS TV, we achieved penetration rates of 16% and 11%, respectively, across all markets where we have been selling these services.

## Wholesale

Wholesale revenues are earned from long distance and other competing carriers who use our local exchange facilities to provide usage services to their customers. Switched access revenues are derived from fixed and usage-based charges paid by carriers for access to our local network. Special access revenues originate from carriers that buy dedicated local exchange capacity to support their private networks. Wholesale services also include local wholesale revenues from unbundled network elements (UNEs), interconnection revenues from competitive local exchange carriers (CLECs) and wireless carriers, and some data transport revenues.

In the first quarter of 2007, our wholesale revenues decreased by \$67 million, or 3.2% compared to the similar period in 2006, due to declines in legacy Verizon switched access revenues and local wholesale revenues, offset by increases in special access revenues.

Switched MOUs declined in the first quarter of 2007 compared to the similar period in 2006, reflecting the impact of access line loss and wireless substitution. Wholesale lines decreased by 16.5% due to the ongoing impact of a 2005 decision by a major competitor to deemphasize their local market initiatives. Special access revenue growth reflects continuing demand in the small business market for high-capacity, high-speed digital services, partially offset by lower demand for older, low-speed data products and services. Customer demand for high-capacity and digital data services increased 9.0% in the first quarter of 2007 compared to the similar period in 2006.

The FCC regulates the rates that we charge customers for interstate access services. See [Other Factors That May Affect Future Results](#) [Regulatory and Competitive Trends](#) [FCC Regulation](#) for additional information on FCC rulemaking concerning federal access rates, universal service and certain broadband services.

## Other Revenues

Our other services include such services as operator services (including deaf relay services), public (coin) telephone, card services and supply sales, as well as dial around services including 10-10-987, 10-10-220, 1-800-COLLECT and Prepaid Cards.

Verizon Telecom's revenues from other services in the first quarter of 2007 decreased by \$136 million, or 22.0% compared to the similar period in 2006. This revenue decrease was mainly due to the discontinuation of non-strategic businesses and reduced business volumes.

## Table of Contents

### *Verizon Business*

#### Enterprise Business

Our Enterprise Business market provides voice, data and internet communications services to medium and large business customers, multi-national corporations, and state and federal government customers. In addition to communication services, this line of business provides value-added services that make communications more secure, reliable and efficient. Enterprise Business provides managed network services for customers that outsource all or portions of their communications and information processing operations and data services such as Private Line, Frame Relay and ATM services, both domestically and internationally.

Enterprise Business first quarter 2007 revenues of \$3,571 million increased \$188 million, or 5.6% compared to the similar period in 2006. The year over year increase reflects the inclusion of the former MCI for the full quarter in 2007. The growth is also driven by our Internet suite of products, specifically Private IP and Voice over Internet Protocol (VoIP). The Internet suite of products is Enterprise Business's fastest growing suite of products and includes Private IP, IP VPN, Web Hosting and VoIP. Enterprise Business contains many customer accounts that are moving from core data products to more robust IP products. This shift in technology is occurring with a few large customers but is predominately driven by many smaller customer accounts.

#### Wholesale

Our Wholesale revenues relate to domestic wholesale services, which include all wholesale traffic sold in the United States, as well as international traffic that originates in the United States. The Wholesale line of business is comprised of numerous large and small customers that predominately resell voice services to their own customer base. Although this line of business contains numerous customers, the majority of revenue is generated by a few large telecommunication carriers many of whom directly compete with Verizon.

In the quarter ended March 31, 2007, our Wholesale revenues of \$850 million increased \$46 million, or 5.7% compared to the first quarter of 2006. The year over year increase reflects the inclusion of the former MCI for the full quarter in 2007. Increased MOUs in traditional voice products partially offset continued rate compression due to competition in the marketplace.

#### International and Other

Our International operations serve businesses, government entities and telecommunication carriers outside of the United States, primarily in Europe, the Middle East and Africa (collectively, EMEA), the Asia Pacific region, Latin America and Canada. This line of business provides telecommunications services, which include voice, data services, Internet and managed network services.

International and other revenues in the quarter ended March 31, 2007 of \$798 million, increased \$61 million or 8.3% versus the prior year quarter. The year over year increase reflects the inclusion of the former MCI for the full quarter in 2007 and strong growth in our Internet suite of products, specifically Private IP products. Partially offsetting growth in the Private IP product was competitive rate compression in our voice products on slightly higher minute volumes.

**Table of Contents****Operating Expenses**

| (Dollars in Millions)                       | Three Months Ended March 31, |           | % Change |
|---|------------------------------|-----------|----------|
|   | 2007                         | 2006      |          |
| Cost of services and sales                  | \$ 6,173                     | \$ 6,055  | 1.9      |
| Selling, general and administrative expense | 2,901                        | 2,953     | (1.8)    |
| Depreciation and amortization expense       | 2,267                        | 2,381     | (4.8)    |
|   | \$ 11,341                    | \$ 11,389 | (0.4)    |

*Cost of Services and Sales*

Cost of services and sales includes the following costs directly attributable to a service or product: salaries and wages, benefits, materials and supplies, contracted services, network access and transport costs, customer provisioning costs, computer systems support, costs to support our outsourcing contracts and technical facilities, contributions to the universal service fund, customer provisioning costs and cost of products sold. Aggregate customer care costs, which include billing and service provisioning, are allocated between cost of services and sales and selling, general and administrative expense.

Cost of services and sales increased by \$118 million, or 1.9% in the first quarter of 2007 compared to the similar period in 2006. This increase was primarily due to the inclusion of the former MCI for the full quarter in 2007, higher costs associated with our growth businesses and annual wage increases partially offset by productivity improvement initiatives, which reduced cost of services and sales expenses in the current period. Costs in this period were also impacted by decreased net pension and other postretirement benefit costs. As of December 31, 2006, we evaluated key employee benefit plan assumptions in response to current conditions in the securities markets. The overall impact of the 2007 assumptions, combined with the impact of the management pension freeze, effective June 30, 2006, resulted in pension and other postretirement benefit expense of \$343 million (primarily in cost of services and sales) in the first quarter of 2007 compared to \$374 million in the first quarter of 2006.

*Selling, General and Administrative Expense*

Selling, general and administrative expense includes salaries and wages and benefits not directly attributable to a service or product, bad debt charges, taxes other than income, advertising and sales commission costs, customer billing, call center and information technology costs, professional service fees and rent for administrative space.

Selling, general and administrative expenses in the first quarter of 2007 decreased by \$52 million, or 1.8% compared to the similar periods in 2006. This decrease was primarily due to lower bad debt costs and cost reduction initiatives, partially offset by higher advertising costs and the inclusion of the former MCI for the full quarter in 2007.

*Depreciation and Amortization Expense*

The decrease in depreciation and amortization expense of \$114 million, or 4.8% in the first quarter of 2007 compared to the similar period in 2006 was mainly driven by lower rates of depreciation as a result of changes in the estimated useful lives of certain asset classes, partially offset by growth in depreciable telephone plant. Amortization expense increased by \$11 million in the first quarter of 2007 compared to the similar period in 2006.

**Segment Income**

| (Dollars in Millions) | Three Months Ended March 31, |        | % Change |
|-----------------------|------------------------------|--------|----------|
|                       | 2007                         | 2006   |          |
| Segment Income        | \$ 365                       | \$ 318 | 14.8     |



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Segment income increased by \$47 million, or 14.8% in the first quarter of 2007 compared to the similar periods in 2006, due to the after-tax impact of operating revenues and operating expenses described above.

Special and non-recurring items not included in Verizon Wireline's segment income totaled \$8.6 million and \$60 million in the first quarter of 2007 and 2006, respectively. Special and non-recurring items in the first quarter of 2007 included costs associated with continued merger integration initiatives. Special and non-recurring items in the first quarter of 2006 included Verizon Center relocation-related costs, merger integration costs and costs associated with the redemption and refinancing of debt assumed in connection with the MCI acquisition.

**Table of Contents****Domestic Wireless**

Our Domestic Wireless segment provides wireless voice and data services and other value added services and equipment sales across the United States. This segment primarily represents the operations of the Verizon Wireless joint venture with Vodafone.

**Operating Revenues**

| (Dollars in Millions)       | Three Months Ended March 31, |          |          |
|-----------------------------|------------------------------|----------|----------|
|                             | 2007                         | 2006     | % Change |
| Wireless sales and services | \$ 10,307                    | \$ 8,813 | 17.0     |

Domestic Wireless's total revenues increased by \$1,494 million, or 17.0% in the first quarter of 2007 compared to the similar period in 2006. Service revenue of \$8,991 million increased by \$1,382 million, or 18.2% in the first quarter of 2007 compared to the similar period in 2006, primarily due to a 14.5% increase in customers and an increase in average revenue per customer per month. Equipment and other revenue increased by \$112 million, or 9.3% in the first quarter of 2007 compared to the first quarter of 2006, principally as a result of an increase in new customers and existing customers upgrading their handsets in exchange for contract extensions. Other revenue increased due to increases in revenue associated with regulatory fees, primarily the universal service fund, and cost recovery surcharges.

Our Domestic Wireless segment ended the first quarter of 2007 with approximately 58.5 million retail customers, compared to 50.7 million retail customers at the end of the first quarter of 2006, an increase of 15.4%. Domestic Wireless added approximately 1.7 million total customers, of which approximately 1.6 million were retail customers, during the first quarter of 2007, unchanged compared to the first quarter of 2006. Approximately 1.5 million of the 1.6 million new retail customers added during the first quarter of 2007 were added through the postpaid channel. The average monthly retail churn rate, the rate at which retail customers disconnect service, was 1.08% during the first quarter of 2007, unchanged compared to the first quarter of 2006. Retail postpaid churn decreased to 0.89% in the first quarter of 2007 compared to 0.92% in the first quarter of 2006. Total customers as of March 31, 2007 were approximately 60.7 million, of which 96% were retail customers.

Average retail service revenue per retail customer per month increased 2.8% to \$50.73 in the first quarter of 2007 compared to the similar period in 2006. Average retail data revenue per retail customer per month increased 54% in the first quarter of 2007, compared to the first quarter of 2006, driven by increased use of our messaging, *VZAccess* and other data services. Retail data revenues were \$1,548 million and accounted for 17.6% of retail service revenue in the first quarter of 2007, compared to \$868 million and 11.8% of retail service revenue in the first quarter of 2006.

**Operating Expenses**

| (Dollars in Millions)                       | Three Months Ended March 31, |          |          |
|---|------------------------------|----------|----------|
|   | 2007                         | 2006     | % Change |
| Cost of services and sales                  | \$ 3,022                     | \$ 2,665 | 13.4     |
| Selling, general and administrative expense | 3,300                        | 2,759    | 19.6     |
| Depreciation and amortization expense       | 1,256                        | 1,274    | (1.4)    |
|   | \$ 7,578                     | \$ 6,698 | 13.1     |

*Cost of Services and Sales*

Cost of services and sales, which are costs to operate the wireless network, as well as the cost of roaming, long distance and equipment sales, increased by \$357 million, or 13.4% in the first quarter of 2007 compared to the similar period in 2006. Cost of services increased by 10.8% due to higher wireless network costs in the first quarter of 2007 caused by increased network usage relating to both voice and data usage, partially offset by lower local interconnection, long distance and roaming rates. Cost of equipment sales increased by 15.3% in the first quarter of 2007 compared to the similar period in 2006. This increase was primarily attributed to an increase in customers and equipment upgrades.

*Selling, General and Administrative Expense*

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Selling, general and administrative expenses increased by \$541 million, or 19.6% in the first quarter of 2007 compared to the similar period in 2006. This increase was primarily due to an increase in salary and benefits expense of \$367 million, principally driven by a \$201 million increase in costs related to our long-term incentive program, an increase in employees primarily in the sales and customer care areas, and higher per employee salary and benefit costs. Sales commission expense in both our direct and indirect channels increased \$59 million in the first quarter of 2007, compared to the similar period in 2006, primarily as a result of the increase in gross customer additions and customer renewals and equipment upgrades. Also

**Table of Contents**

contributing to this increase in expenses was a \$20 million increase in costs associated with regulatory fees, primarily universal service fund fees, in the first quarter of 2007 compared to the similar period in 2006.

*Depreciation and Amortization Expense*

Depreciation and amortization expense decreased by \$18 million, or 1.4% in the first quarter of 2007 compared to the similar period in 2006. This decrease consisted of lower amortization expense, due to fully amortized customer lists, partially offset by increases in depreciation expense related to an increase in depreciable assets.

**Segment Income**

| (Dollars in Millions) | Three Months Ended March 31, |        |          |
|-----------------------|------------------------------|--------|----------|
|                       | 2007                         | 2006   | % Change |
| Segment Income        | \$ 874                       | \$ 631 | 38.5     |

Segment income increased by \$243 million, or 38.5% in the first quarter of 2007 compared to the similar period in 2006 primarily as a result of the after-tax impact of the changes in operating revenues and operating expenses described above, partially offset by an increase in minority interest. The minority interest relates primarily to the significant minority interest attributable to Vodafone. Segment results exclude certain special and non-recurring items. There were no special and non-recurring items in the first quarter of 2007. The special and non-recurring items in the first quarter of 2006 were \$42 million related to the cumulative effect in accounting change for the adoption of SFAS 123(R), as described in the consolidated results above.

**Special and Non-Recurring Items****Disposition of Businesses***Telecomunicaciones de Puerto Rico, Inc.*

On March 27, 2007, the Federal Communications Commission approved the sale of Telecomunicaciones de Puerto Rico, Inc. (TELPRI) to América Móvil, S.A.B. de C.V. (América Móvil). On March 30, 2007, we completed the previously announced sale of our interest in TELPRI to a subsidiary of América Móvil and recorded a pretax gain of \$120 million (\$70 million after-tax, or \$.02 per diluted share). América Móvil purchased 100% of TELPRI, the holding company of Puerto Rico Telephone Company, including Verizon's 52% interest. As a result of this sale transaction, Verizon contributed \$100 million to Verizon Foundation to fund its charitable activities and increase its self-sufficiency.

*Compañía Anónima Nacional Teléfonos de Venezuela*

In January 2007, the Bolivarian Republic of Venezuela (the Republic) declared its intent to nationalize certain companies, including CANTV. On February 12, 2007, we entered into a Memorandum of Understanding (MOU) with the Republic. The MOU provides that the Republic will offer to purchase all of the equity securities of CANTV, including our 28.5% interest, through public tender offers in Venezuela and the United States at a price equivalent to \$17.85 per American Depository Share (ADS), subject to adjustment if CANTV declared and paid a dividend prior to the purchase of the equity securities in the tender offers. A dividend of 6,454.49 Bolivars per ADS (equivalent to \$3.00 at the current official exchange rate) with an April 18, 2007 payment date was recommended by the CANTV Board and then approved by shareholders on March 30, 2007. The Republic launched the public tender offers on April 9, 2007 at a price equivalent to \$14.85 per ADS. Unless extended, the offers will expire on May 8, 2007. The price is subject to further adjustment for any additional dividends declared and paid before the date the equity securities are accepted for payment, and in the event of a change in the official exchange rate, for changes to the equivalent dollar value of the April 18 dividend. The tender offers are subject to certain conditions including that a majority of the outstanding shares are tendered to the

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Republic. Based upon the terms of the MOU and our current investment balance in CANTV, we recorded an extraordinary loss on our investment of \$131 million, net of tax, or \$.05 per diluted share, in the first quarter of 2007. If the tender offers are completed, Verizon expects to receive an aggregate amount of \$572 million through a combination of purchase price and the 2007 dividend.

**Table of Contents****Merger Integration Costs**

During the first quarter of 2007, we recorded pretax charges of \$14 million (\$9 million after-tax) related to integration costs associated with the MCI acquisition that closed on January 6, 2006. These costs are primarily comprised of systems integration activities.

During the first quarter of 2006, we recorded pretax charges of \$55 million (\$35 million after-tax, or \$.01 per diluted share) related to integration costs associated with the MCI acquisition that primarily comprised of advertising and other costs related to re-branding initiatives and systems integration activities.

**Facility and Other Special Items**

During the first quarter of 2006, we recorded pretax charges of \$46 million (\$28 million after-tax, or \$.01 per diluted share) in connection with the relocation of several functions to Verizon Center located in Basking Ridge, New Jersey.

In addition, during the first quarter of 2006 we recorded pretax charges of \$26 million (\$16 million after-tax, or \$.01 per diluted share) resulting from the extinguishment of debt assumed in connection with the completion of the MCI merger.

**Consolidated Financial Condition**

| (Dollars in Millions)                                   | <b>Three Months Ended March 31,</b> |               |                   |
|---|-------------------------------------|---------------|-------------------|
|   | <b>2007</b>                         | <b>2006</b>   | <b>Change</b>     |
| <b>Cash Flows Provided By (Used In)</b>                 |                                     |               |                   |
| Operating activities                                    | \$ 4,517                            | \$ 6,066      | \$ (1,549)        |
| Investing activities                                    | (3,187)                             | (1,748)       | (1,439)           |
| Financing activities                                    | (3,248)                             | (3,830)       | 582               |
| <b>Increase (Decrease) In Cash and Cash Equivalents</b> | <b>\$ (1,918)</b>                   | <b>\$ 488</b> | <b>\$ (2,406)</b> |

We use the net cash generated from our operations to fund network expansion and modernization, repay external financing, pay dividends and invest in new businesses. Additional external financing is utilized when necessary. While our current liabilities typically exceed current assets, our sources of funds, primarily from operations and, to the extent necessary, from readily available external financing arrangements, are sufficient to meet ongoing operating and investing requirements. We expect that capital spending requirements will continue to be financed primarily through internally generated funds. Additional debt or equity financing may be needed to fund additional development activities or to maintain our capital structure to ensure our financial flexibility.

**Cash Flows Provided By Operating Activities**

Our primary source of funds continues to be cash generated from operations. The decrease in cash from operating activities for the three months ended March 31, 2007 compared to the similar period of 2006 was primarily due to a decline in cash collections, as well as an increase in inventory of high demand data capable devices. Partially offsetting the decline in operating cash flow was a decline in interest payments, as a

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result of lower average debt balances and interest rates, and increased cash as a result of changes in working capital and higher operating income.

Operating cash flows used in discontinued operations was \$527 million during the first quarter of 2007 primarily due to income taxes paid related to the fourth quarter 2006 disposition of Verizon Dominicana, as well as the absence of operating activities for other assets that were disposed of in the fourth quarter of 2006.

## **Table of Contents**

### **Cash Flows Used In Investing Activities**

Capital expenditures continue to be our primary use of capital resources as they facilitate the introduction of new products and services, enhance responsiveness to competitive challenges and increase the operating efficiency and productivity of our networks. Including capitalized software, we invested \$2,439 million in our Wireline business during the first quarter of 2007, compared to \$2,418 million in the similar period of 2006. In the first quarter of 2007, we also invested \$1,721 million in our Domestic Wireless business, compared with \$1,581 million in the first quarter of 2006.

In the first quarter of 2007, we invested \$124 million primarily for acquisitions of wireless licenses. During the first quarter of 2006, we received net cash proceeds of \$1,526 million from acquisitions and investments in businesses, primarily driven by MCI's cash balances at the date of the merger. Other, net investing activities in the first quarter of 2007 and 2006 includes cash proceeds from the sale of buildings and disposition of select non-strategic assets.

In the first quarter of 2007, discontinued operations primarily included gross proceeds of approximately \$980 million in connection with the sale of TELPRI.

Under the terms of an investment agreement, as of December 31, 2006, Vodafone has the right to require the purchase of up to \$10 billion worth of its interest in Verizon Wireless, during a 61-day period opening on June 10 and closing on August 9 in 2007, under its one remaining put window. Vodafone also may require that Verizon Wireless pay for up to \$7.5 billion of the required repurchase through the assumption or incurrence of debt. In the event Vodafone fully exercises its one remaining put right, we (instead of Verizon Wireless) have the right, exercisable at our sole discretion, to purchase up to \$2.5 billion of the \$10 billion Vodafone interest for cash or Verizon stock at our option.

### **Cash Flows Used In Financing Activities**

Our total debt was reduced by \$1,684 million during the first three months of 2007. We repaid \$725 million of Wireline debt, including the early repayment of previously guaranteed \$300 million 7.0% debentures issued by Verizon South Inc. Also, we redeemed \$1,580 million principal of our outstanding floating rate notes, which were callable by Verizon on or after August 15, 2006, and the \$500 million 7.90% debentures issued by GTE Corporation. Our ratio of debt to debt combined with shareowners' equity was 41.5% at March 31, 2007 compared to 42.8% at December 31, 2006.

As of March 31, 2007, we had no bank borrowings outstanding. We also had approximately \$6.2 billion of unused bank lines of credit (including a \$6.0 billion three-year committed facility that expires in September 2009 and various other facilities totaling approximately \$400 million) and we had shelf registrations for the issuance of up to \$4.5 billion of unsecured debt securities. The debt securities of Verizon and our telephone subsidiaries continue to be accorded high ratings by primary rating agencies. Verizon Communications is the primary issuer of all long-term and short-term debt for Verizon. The short-term ratings of Verizon Communications are: Moody's P-2; S&P A-1; and Fitch F1. The long-term ratings of Verizon Communications are: Moody's A3 with stable outlook; S&P A with negative outlook; and Fitch A+ with stable outlook. Following the maturity of its remaining external debt in December 2006, Moody's and Fitch withdrew the rating on Verizon Wireless.

We and our consolidated subsidiaries are in compliance with all of our debt covenants.

As in prior periods, dividend payments were a significant use of capital resources. We determine the appropriateness of the level of our dividend payments on a periodic basis by considering such factors as long-term growth opportunities, internal cash requirements and the expectations of our shareowners. In the first quarter of 2007 and 2006, Verizon declared quarterly cash dividends of \$.405 per share.

### **Increase (Decrease) In Cash and Cash Equivalents**



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Our cash and cash equivalents at March 31, 2007 totaled \$1,301 million, a \$1,918 million decrease compared to cash and cash equivalents at December 31, 2006 of \$3,219 million.

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## **Table of Contents**

### **Market Risk**

We are exposed to various types of market risk in the normal course of business, including the impact of interest rate changes, foreign currency exchange rate fluctuations, changes in equity investment and commodity prices and changes in corporate tax rates. We employ risk management strategies using a variety of derivatives, including interest rate swap agreements, interest rate locks, foreign currency forwards, commodity swaps and equity options. We do not hold derivatives for trading purposes.

It is our general policy to enter into interest rate, foreign currency and other derivative transactions only to the extent necessary to achieve our desired objectives in limiting our exposures to the various market risks. Our objectives include maintaining a mix of fixed and variable rate debt to lower borrowing costs within reasonable risk parameters and to protect against earnings and cash flow volatility resulting from changes in market conditions. We do not hedge our market risk exposure in a manner that would completely eliminate the effect of changes in interest rates, equity or commodity prices and foreign exchange rates on our earnings. We do not expect that our net income, liquidity and cash flows will be materially affected by these risk management strategies.

### **Foreign Currency Translation**

The functional currency for our foreign operations is primarily the local currency. The translation of income statement and balance sheet amounts of our foreign operations into U.S. dollars are recorded as cumulative translation adjustments, which are included in Accumulated Other Comprehensive Loss in our consolidated balance sheets. The translation gains and losses of foreign currency transactions and balances are recorded in the consolidated statements of income in Other Income and (Expense), Net and Income from Discontinued Operations, Net of Tax. At March 31, 2007, our primary translation exposure was to the British Pound and the Euro.

### **Other Factors That May Affect Future Results**

### **Recent Developments**

#### *Telephone Access Lines Spin-off*

On January 16, 2007, we announced a definitive agreement with FairPoint Communications, Inc. (FairPoint) that will result in Verizon establishing a separate entity for its local exchange and related business assets in Maine, New Hampshire and Vermont, spinning off that new entity to Verizon's shareowners, and immediately merging it with and into FairPoint. These local exchange and business assets are included in Verizon's continuing operations. The transaction is subject to the satisfaction of certain conditions, including receipt of state and federal telecommunications regulatory approvals. We expect this transaction to close within one year of the date of announcement.

Upon the closing of the transaction, Verizon shareowners will own approximately 60 percent of the new company and FairPoint stockholders will own approximately 40 percent. Verizon Communications will not own any shares in FairPoint after the merger. In connection with the merger, Verizon shareowners will receive one share of FairPoint stock for approximately every 55 shares of Verizon stock held as of the record date. Both the spin-off and merger are expected to qualify as tax-free transactions, except to the extent that cash is paid to Verizon shareowners in lieu of fractional shares.

The total value to be received by Verizon and its shareowners in exchange for these operations will be approximately \$2,715 million. Verizon shareowners will receive approximately \$1,015 million of FairPoint common stock in the merger, based upon FairPoint's recent stock price and the terms of the merger agreement. Verizon will receive \$1,700 million in value through a combination of cash distributions to Verizon and debt securities issued to Verizon prior to the spin-off. Verizon may exchange these newly issued debt securities for certain debt that was previously

issued by Verizon, which would have the effect of reducing Verizon's then-outstanding debt.

**Environmental Matters**

During 2003, under a government-approved plan, remediation commenced at the site of a former Sylvania facility in Hicksville, New York that processed nuclear fuel rods in the 1950s and 1960s. Remediation beyond original expectations proved to be necessary and a reassessment of the anticipated remediation costs was conducted. A reassessment of costs related to remediation efforts at several other former facilities was also undertaken. As a result, an additional environmental remediation expense of \$240 million was recorded in 2003, for remedial activities likely to take place over the next several years. In September 2005, the Army Corps of Engineers (ACE) accepted the Hicksville site into the

**Table of Contents**

Formerly Utilized Sites Remedial Action Program. This may result in the ACE performing some or all of the remaining remediation effort for the Hicksville site with a corresponding decrease in costs to Verizon. To the extent that the ACE assumes responsibility for remedial work at the Hicksville site, an adjustment to the remaining reserve may be necessary. Adjustments may also be made based upon actual conditions discovered during the remediation at any of the other sites requiring remediation.

**New York Recovery Funding**

In August 2002, President Bush signed the Supplemental Appropriations bill that included \$5.5 billion in New York recovery funding. Of that amount, approximately \$750 million has been allocated to cover utility restoration and infrastructure rebuilding as a result of the September 11th terrorist attacks on lower Manhattan. These funds will be distributed through the Lower Manhattan Development Corporation following an application and audit process. As of September 2004, we had applied for reimbursement of approximately \$266 million under Category One and in 2004 and 2005 we applied for reimbursement of an additional \$139 million of Category Two losses. Category One funding relates to Emergency and Temporary Service Response while Category Two funding is for permanent restoration and infrastructure improvement. According to the plan, permanent restoration is reimbursed up to 75% of the loss. On November 3, 2005, we received the results of preliminary audit findings disallowing all but \$49.9 million of our \$266 million of Category One application. On December 8, 2005, we provided a detailed rebuttal to the preliminary audit findings. We received a copy of the final audit report for Verizon's Category One applications and, on January 4, 2007, we filed an appeal of the final audit report. That appeal, as well as our Category Two applications, are pending.

**FASB Interpretation No. 48**

Effective January 1, 2007, we adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48), which requires the use of a two-step approach for recognizing and measuring tax benefits taken or expected to be taken in a tax return and disclosures regarding uncertainties in income tax positions. As a result of the implementation of FIN 48, we recorded adjustments to liabilities that resulted in a net \$79 million increase in the liability for unrecognized tax benefits with an offsetting reduction to retained earnings as of January 1, 2007. The implementation of FIN 48 also resulted in adjustments to prior acquisitions accounted for under purchase accounting, resulting in a \$635 million reduction in the liability for unrecognized tax benefits and corresponding reductions to goodwill and wireless licenses of \$100 million and \$535 million, respectively. The implementation impact included a reduction in Deferred income taxes of approximately \$3 billion, offset with a similar increase in Other liabilities as of January 1, 2007.

The total amount of unrecognized tax benefits at January 1, 2007, is \$2,958 million. Included in the total unrecognized tax benefits is \$1,290 million that, if recognized would favorably affect the effective tax rate. The remaining unrecognized tax benefits relate to temporary items that would not affect the annual effective tax rate and uncertain tax positions resulting from prior acquisitions which, pursuant to current purchase accounting tax rules, would adjust goodwill.

We recognize any interest and penalties accrued related to unrecognized tax benefits in income tax expense. We had approximately \$444 million (after-tax) for the payment of interest and penalties accrued in the balance sheet at January 1, 2007, relating to the \$2,958 million unrecognized tax benefits reflected above. We had approximately \$486 million (after-tax) for the payment of interest and penalties accrued in the balance sheet at March 31, 2007.

Verizon or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction, and various state and local and foreign jurisdictions. The Company is generally no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2000. The Internal Revenue Service (IRS) is currently examining the Company's U.S. income tax returns for years 2000 through 2003. We do not anticipate any significant increase or decrease to the unrecognized tax benefits within the next twelve months.

**FASB Staff Position FAS 13-2**

FASB Staff Position FAS 13-2, *Accounting for a Change or Projected Change in the Timing of Cash Flows Relating to Income Taxes Generated by a Leveraged Lease Transaction* (FSP 13-2) requires that changes in the projected timing of income tax cash flows generated by a leveraged lease transaction be recognized as a gain or loss in the year in which the change occurs. We adopted FSP 13-2 effective January 1, 2007. The cumulative effect of initially adopting FSP 13-2 was a reduction to retained earnings of \$55 million, after-tax. There was no impact on our condensed consolidated income statement.

## **Table of Contents**

### **Regulatory and Competitive Trends**

#### **Competition and Regulation**

Technological, regulatory and market changes have provided Verizon both new opportunities and challenges. These changes have allowed Verizon to offer new types of services in this increasingly competitive market. At the same time, they have allowed other service providers to broaden the scope of their own competitive offerings. Current and potential competitors for network services include other telephone companies, cable companies, wireless service providers, foreign telecommunications providers, satellite providers, electric utilities, Internet service providers, providers of VoIP services, and other companies that offer network services using a variety of technologies. Many of these companies have a strong market presence, brand recognition and existing customer relationships, all of which contribute to intensifying competition and may affect our future revenue growth. Many of our competitors also remain subject to fewer regulatory constraints than Verizon.

We are unable to predict definitively the impact that the ongoing changes in the telecommunications industry will ultimately have on our business, results of operations or financial condition. The financial impact will depend on several factors, including the timing, extent and success of competition in our markets, the timing and outcome of various regulatory proceedings and any appeals, and the timing, extent and success of our pursuit of new opportunities.

#### **FCC Regulation**

Our services are subject to the jurisdiction of the FCC with respect to interstate telecommunications services and other matters for which the FCC has jurisdiction under the Communications Act of 1934, as amended (Communications Act). The Communications Act generally obligates us not to charge unjust or unreasonable rates nor engage in unreasonable discrimination when we are providing services as a common carrier, and regulates some of the rates, terms and conditions under which we provide certain services. The FCC also has adopted regulations governing various aspects of our business, such as the following: (i) use and disclosure of customer proprietary network information; (ii) telemarketing; (iii) assignment of telephone numbers to customers; (iv) provision to law enforcement agencies of the capability to obtain call identifying information and call content information from calls pursuant to lawful process; (v) accessibility of services and equipment to individuals with disabilities if readily achievable; (vi) interconnection with the networks of other carriers; and (vii) customers' ability to keep (or port) their telephone numbers when switching to another carrier. In addition, we pay various fees to support other FCC programs, such as the universal service program discussed below. Changes to these mandates, or the adoption of additional mandates, could require us to make changes to our operations or otherwise increase our costs of compliance.

#### *Broadband*

The FCC has adopted a series of orders that recognize the competitive nature of the broadband market, and impose lesser regulatory requirements on broadband services and facilities than apply to narrowband. With respect to facilities, the FCC has determined that certain unbundling requirements that apply to narrowband facilities do not apply to broadband facilities such as fiber to the premise loops and packet switches. With respect to services, the FCC has concluded that broadband Internet access services offered by telephone companies and their affiliates qualify as largely deregulated information services. The same order also concluded that telephone companies may offer the underlying broadband transmission services that are used as an input to Internet access services through private carriage arrangements on negotiated commercial terms. In addition, a Verizon petition asking the FCC to forbear from applying common carrier regulation to certain broadband services sold primarily to larger business customers when those services are not used for Internet access was deemed granted by operation of law on March 19, 2006 when the FCC did not deny the petition by the statutory deadline. Both the FCC's order addressing the appropriate regulatory treatment of broadband Internet access services and the relief obtained through the forbearance petition are the subject of pending appeals.

#### *Video*

The FCC has a body of rules that apply to cable operators under Title VI of the Communications Act of 1934, and these rules also generally apply to telephone companies that provide cable services over their networks. In addition, companies that provide cable service over a cable system generally must obtain a local cable franchise. On March 5, 2007, the FCC released an order setting forth parameters consistent with Section 621 of the Communications Act of 1934 and other federal law, on the timing and scope of franchise negotiations by local franchising authorities. The Commission found that some prior practices in the local franchise approval process constituted an unreasonable refusal to award a competitive local franchise under the requirements of federal law. This order is the subject of a pending appeal.



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**Table of Contents**

*Interstate Access Charges and Intercarrier Compensation*

The current framework for interstate access rates was established in the Coalition for Affordable Local and Long Distance Services (CALLS) plan, which the FCC adopted on May 31, 2000. The CALLS plan has three main components. First, it establishes portable interstate access universal service support of \$650 million for the industry that replaces implicit support previously embedded in interstate access charges. Second, the plan simplifies the patchwork of common line charges into one subscriber line charge (SLC) and provides for de-averaging of the SLC by zones and class of customers. Third, the plan set into place a mechanism to transition to a set target of \$.0055 per minute for switched access services. Once that target rate is reached, local exchange carriers are no longer required to make further annual price cap reductions to their switched access prices. As a result of tariff adjustments which became effective in July 2003, virtually all of our switched access lines reached the \$.0055 benchmark.

The FCC currently is conducting a broad rulemaking proceeding to consider new rules governing intercarrier compensation including, but not limited to, access charges, compensation for Internet traffic, and reciprocal compensation for local traffic. The FCC has sought comments about intercarrier compensation in general, and requested input on a number of specific reform proposals.

The FCC also has pending before it issues relating to intercarrier compensation for dial-up Internet-bound traffic. The FCC previously found that this traffic is not subject to reciprocal compensation under Section 251(b)(5) of the Telecommunications Act of 1996. Instead, the FCC established federal rates per minute for this traffic that declined from \$.0015 to \$.0007 over a three-year period, established caps on the total minutes of this traffic subject to compensation in a state, and required incumbent local exchange carriers to offer to both bill and pay reciprocal compensation for local traffic at the same rate as they are required to pay on Internet-bound traffic. The U.S. Court of Appeals for the D.C. Circuit rejected part of the FCC's rationale, but declined to vacate the order while it is on remand. As a result, pending further action by the FCC, the FCC's underlying order remains in effect. The FCC subsequently denied a petition to discontinue the \$.0007 rate cap on this traffic, but removed the caps on the total minutes of Internet-bound traffic subject to compensation. That decision has been upheld on appeal. Disputes also remain pending in a number of forums relating to the appropriate compensation for Internet-bound traffic during previous periods under the terms of our interconnection agreements with other carriers.

The FCC also is conducting a rulemaking proceeding to address the regulation of services that use Internet protocol, including whether access charges should apply to voice or other Internet protocol services. The FCC also considered several petitions asking whether, and under what circumstances, services that employ Internet protocol are subject to access charges. The FCC previously has held that one provider's peer-to-peer Internet protocol service that does not use the public switched network is an interstate information service and is not subject to access charges, while a service that utilizes Internet protocol for only one intermediate part of a call's transmission is a telecommunications service that is subject to access charges. Another petition asking the FCC to forbear from applying access charges to voice over Internet protocol services that are terminated on switched local exchange networks was withdrawn by the carrier that filed that petition. The FCC also declared the services offered by one provider of a voice over Internet protocol service to be jurisdictionally interstate on the grounds that it was impossible to separate that carrier's Internet protocol service into interstate and intrastate components. The FCC also stated that its conclusion would apply to other services with similar characteristics. On March 21, 2007, the Eighth Circuit Court of Appeals affirmed the FCC's Order.

The FCC also has adopted rules for special access services that provide for pricing flexibility and ultimately the removal of services from price regulation when prescribed competitive thresholds are met. More than half of special access revenues are now removed from price regulation. The FCC currently has a rulemaking proceeding underway to evaluate experience under its pricing flexibility rules, and to determine whether any changes to those rules are warranted.

*Universal Service*

The FCC also has a body of rules implementing the universal service provisions of the Telecommunications Act of 1996, including rules governing support to rural and non-rural high-cost areas, support for low income subscribers, and support for schools, libraries and rural health care. The FCC's current rules for support to high-cost areas served by larger non-rural local telephone companies were previously remanded by U.S. Court of Appeals for the Tenth Circuit, which had found that the FCC had not adequately justified these rules. The FCC has initiated a rulemaking proceeding in response to the court's remand, but its rules remain in effect pending the results of the rulemaking. The FCC also has proceedings underway to evaluate possible changes to its current rules for assessing contributions to the universal service fund. As an interim step, in June 2006, the FCC ordered that providers of VoIP services are subject to federal universal service obligations. The FCC also increased the percentage of revenues subject to federal universal service obligations that wireless providers may use as a safe harbor. This order has been appealed. Any further change in the current assessment

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**Table of Contents**

mechanism could result in a change in the contribution that local telephone companies, wireless carriers or others must make and that would have to be collected from customers.

*Unbundling of Network Elements*

Under Section 251 of the Telecommunications Act of 1996, incumbent local exchange carriers were required to provide competing carriers with access to components of their network on an unbundled basis, known as UNEs, where certain statutory standards are satisfied. The Telecommunications Act of 1996 also adopted a cost-based pricing standard for these UNEs, which the FCC interpreted as allowing it to impose a pricing standard known as total element long run incremental cost or TELRIC. The FCC's rules defining the unbundled network elements that must be made available at TELRIC prices have been overturned on multiple occasions by the courts. In its most recent order issued in response to these court decisions, the FCC eliminated the requirement to unbundle mass market local switching on a nationwide basis, with the obligation to accept new orders ending as of the effective date of the order (March 11, 2005). The FCC also established a one year transition for existing UNE switching arrangements. For high capacity transmission facilities, the FCC established criteria for determining whether high capacity loops, transport or dark fiber transport must be unbundled in individual wire centers, and stated that these standards were only expected to affect a small number of wire centers. The FCC also eliminated the obligation to provide dark fiber loops and found that there is no obligation to provide UNEs exclusively for wireless or long distance service. In any instance where a particular high capacity facility no longer has to be made available as a UNE, the FCC established a similar one year transition for any existing high capacity loop or transport UNEs, and an 18 month transition for any existing dark fiber UNEs. This decision has been upheld on appeal.

As noted above, the FCC has concluded that the requirement under Section 251 of the Telecommunications Act of 1996 to provide unbundled network elements at TELRIC prices generally does not apply with respect to broadband facilities, such as fiber to the premises loops, the packet-switched capabilities of hybrid loops and packet switching. The FCC also has held that any separate unbundling obligations that may be imposed by Section 271 of the Telecommunications Act of 1996 do not apply to these same facilities. The decision with respect to Section 271 has been upheld on appeal and a petition for rehearing of that order was denied.

*Wireless Services*

The FCC regulates the licensing, construction, operation, acquisition and transfer of wireless communications systems, including the systems that Verizon Wireless operates, pursuant to the Communications Act, other legislation, and the FCC's rules. The FCC and Congress continuously consider changes to these laws and rules. Adoption of new laws or rules may raise the cost of providing service or require modification of Verizon Wireless' business plans or operations.

To use the radio frequency spectrum, wireless communications systems must be licensed by the FCC to operate the wireless network and mobile devices in assigned spectrum segments. Verizon Wireless holds FCC licenses to operate in several different radio services, including the cellular radiotelephone service, personal communications service, advanced wireless service, and point-to-point radio service. The technical and service rules, the specific radio frequencies and amounts of spectrum we hold, and the sizes of the geographic areas we are authorized to operate in, vary for each of these services. However, all of the licenses Verizon Wireless holds allow it to use spectrum to provide a wide range of mobile and fixed communications services, including both voice and data services, and Verizon Wireless operates a seamless network that utilizes those licenses to provide services to customers. Because the FCC issues licenses for only a fixed time, generally 10 years, Verizon Wireless must periodically seek renewal of those licenses. Although the FCC has routinely renewed all of Verizon Wireless' licenses that have come up for renewal to date, challenges could be brought against the licenses in the future. If a wireless license were revoked or not renewed upon expiration, Verizon Wireless would not be permitted to provide services on the licensed spectrum in the area covered by that license.

The FCC has also imposed specific mandates on carriers that operate wireless communications systems, which increase Verizon Wireless' costs. These mandates include requirements that Verizon Wireless: (i) meet specific construction and geographic coverage requirements during the license term; (ii) meet technical operating standards that, among other things, limit the radio frequency radiation from mobile devices and antennas; (iii) deploy Enhanced 911 wireless services that provide the wireless caller's number, location and other information upon request by a state or local public safety agency that handles 911 calls; and (iv) comply with regulations for the construction of transmitters and towers that, among other things, restrict siting of towers in environmentally sensitive locations and in places where the towers would affect a site listed or eligible for listing on the National Register of Historic Places. Changes to these mandates could require Verizon Wireless to make changes to operations or increase its costs of compliance.



## **Table of Contents**

The Communications Act imposes restrictions on foreign ownership of U.S. wireless systems. The FCC has approved the interest that Vodafone Group Plc holds, through various of its subsidiaries, in Verizon Wireless. The FCC may need to approve any increase in Vodafone's interest or the acquisition of an ownership interest by other foreign entities. In addition, as part of the FCC's approval of Vodafone's ownership interest, Verizon Wireless, Verizon and Vodafone entered into an agreement with the U.S. Department of Defense, Department of Justice and Federal Bureau of Investigation which imposes national security and law enforcement-related obligations on the ways in which Verizon Wireless stores information and otherwise conducts its business.

Verizon Wireless anticipates that it will need additional spectrum to meet future demand. It can meet spectrum needs by purchasing licenses or leasing spectrum from other licensees, or by acquiring new spectrum licenses from the FCC. Under the Communications Act, before Verizon Wireless can acquire a license from another licensee in order to expand its coverage or its spectrum capacity in a particular area, it must file an application with the FCC, and the FCC can grant the application only after a period for public notice and comment. This review process can delay acquisition of spectrum needed to expand services. The Communications Act also requires the FCC to award new licenses for most commercial wireless services through a competitive bidding process in which spectrum is awarded to bidders in an auction. Verizon Wireless has participated in spectrum auctions to acquire licenses in the personal communication service and most recently the advanced wireless service. However, the timing of future auctions, and the spectrum being sold, may not match Verizon Wireless's needs, and the company may not be able to secure the spectrum in the auction.

The FCC is also conducting several proceedings to explore whether and how to use spectrum more intensively by, for example, allowing unlicensed wireless devices to operate in licensed spectrum bands. These proceedings could increase radio interference to Verizon Wireless's operations from other spectrum users, or allow other users to share its spectrum. These changes may adversely impact the ways in which it uses spectrum, the capacity of that spectrum to carry traffic, and the value of that spectrum.

## **State Regulation and Local Approvals**

### *Telephone Operations*

State public utility commissions regulate our telephone operations with respect to certain telecommunications intrastate rates and services and other matters. Our competitive local exchange carrier and long distance operations are generally classified as nondominant and lightly regulated the same as other similarly situated carriers. Our incumbent local exchange operations are generally classified as dominant. These latter operations predominantly are subject to alternative forms of regulation (AFORs) in the various states, although they remain subject to rate of return regulation in a few states. Arizona, Illinois, Nevada, New Hampshire, Oregon and Washington are rate of return regulated with various levels of pricing flexibility for competitive services. California, Connecticut, Delaware, the District of Columbia, Florida, Indiana, Maryland, Michigan, Maine, Massachusetts, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Rhode Island, South Carolina, Texas, Vermont, Virginia, West Virginia and Wisconsin are under AFORs with various levels of pricing flexibility, detariffing, and service quality standards. None of the AFORs include earnings regulation. In Idaho, Verizon has made the election under a recent statutory amendment into a deregulatory regime that phases out all price regulation.

### *Video*

Companies that provide cable service over a cable system are typically subject to state and/or local cable television rules and regulations. As noted above, cable operators generally must obtain a local cable franchise from each local unit of government prior to providing cable service in that local area. Some states have recently enacted legislation that enables cable operators to apply for, and obtain, a single cable franchise at the state, rather than local, level. To date, Verizon has applied for and received state-issued franchises in California, Indiana, New Jersey, Texas and the unincorporated areas of Delaware. Virginia law provides us the option of entering a given franchise area using state standards if local franchise negotiations are unsuccessful.

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**Table of Contents**

*Wireless Services*

The rapid growth of the wireless industry has led to an increase in efforts by some state legislatures and state public utility commissions to regulate the industry in ways that may impose additional costs on Verizon Wireless. The Communications Act generally preempts regulation by state and local governments of the entry of, or the rates charged by, wireless carriers. Although a state may petition the FCC to allow it to impose rate regulation, no state has done so. In addition, the Communications Act does not prohibit the states from regulating the other terms and conditions of wireless service. While numerous state commissions do not currently have jurisdiction over wireless services, state legislatures may decide to grant them such jurisdiction, and those commissions that already have authority to impose regulations on wireless carriers may adopt new rules.

State efforts to regulate wireless services have included proposals to regulate customer billing, termination of service, trial periods for service, advertising, network outages, the use of handsets while driving, and the provision of emergency or alert services. Over the past several years, only a few states have imposed regulation in one or more of these areas, and in 2006 a federal appellate court struck down one such state statute, but Verizon Wireless expects these efforts to continue. Some states also impose their own universal service support regimes on wireless and other telecommunications carriers, and other states are considering whether to create such regimes.

Verizon Wireless (as well as AT&T (formerly Cingular) and Sprint-Nextel) is a party to an Assurance of Voluntary Compliance (AVC) with 33 State Attorneys General. The AVC, which generally reflected Verizon Wireless's practices at the time it was entered into in July 2004, obligates the company to disclose certain rates and terms during a sales transaction, to provide maps depicting coverage, and to comply with various requirements regarding advertising, billing, and other practices.

At the state and local level, wireless facilities are subject to zoning and land use regulation. Under the Communications Act, neither state nor local governments may categorically prohibit the construction of wireless facilities in any community or take actions, such as indefinite moratoria, which have the effect of prohibiting service. Nonetheless, securing state and local government approvals for new tower sites has been and is likely to continue to be a difficult, lengthy and expensive process. Finally, state and local governments continue to impose new or higher fees and taxes on wireless carriers.

**Other Recent Accounting Pronouncements**

In February 2007, the Financial Accounting Standards Board issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of SFAS 115* (SFAS No. 159), which allows for the option to measure financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of SFAS No. 159 on our consolidated financial statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurement* (SFAS No. 157). SFAS No. 157 expands disclosures about fair value measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and establishes a hierarchy that categorizes and prioritizes the sources to be used to estimate fair value. We are required to adopt SFAS No. 157 effective January 1, 2008 on a prospective basis. We are currently evaluating the impact this new standard will have on our future results of operations and financial position.

In June 2006, the Emerging Task Force (EITF) reached a consensus on EITF No. 06-3, *How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement* (EITF No. 06-3). EITF No. 06-3 permits that such taxes may be presented on either a gross basis or a net basis as long as that presentation is used consistently. The adoption of EITF No. 06-3 on January 1, 2007 did not impact our condensed consolidated financial statements. We present the taxes within the scope of EITF No. 06-3 on a net basis.

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**Table of Contents**

**Cautionary Statement Concerning Forward-Looking Statements**

In this Management's Discussion and Analysis of Financial Condition and Results of Operations, and elsewhere in this Quarterly Report, we have made forward-looking statements. These statements are based on our estimates and assumptions and are subject to risks and uncertainties. Forward-looking statements include the information concerning our possible or assumed future results of operations. Forward-looking statements also include those preceded or followed by the words "anticipates," "believes," "estimates," "hopes" or similar expressions. For those statements, we claim the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

The following important factors, along with those discussed elsewhere in this Quarterly Report, could affect future results and could cause those results to differ materially from those expressed in the forward-looking statements:

materially adverse changes in economic and industry conditions and labor matters, including workforce levels and labor negotiations, and any resulting financial and/or operational impact, in the markets served by us or by companies in which we have substantial investments;

material changes in available technology, including disruption of our suppliers' provisioning of critical products or services;

technology substitution;

an adverse change in the ratings afforded our debt securities by nationally accredited ratings organizations;

the final results of federal and state regulatory proceedings concerning our provision of retail and wholesale services and judicial review of those results;

the effects of competition in our markets;

the timing, scope and financial impacts of our deployment of fiber-to-the-premises broadband technology;

the ability of Verizon Wireless to continue to obtain sufficient spectrum resources;

changes in our accounting assumptions that regulatory agencies, including the SEC, may require or that result from changes in the accounting rules or their application, which could result in an impact on earnings;

the timing of the completion of the sale of our Latin American property; and,

the extent and timing of our ability to obtain revenue enhancements and cost savings following our business combination with MCI, Inc.

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## **Table of Contents**

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Information relating to market risk is included in Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations in the section under the caption "Market Risk."

### **Item 4. Controls and Procedures**

Our chief executive officer and chief financial officer have evaluated the effectiveness of the registrant's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934), as of the end of the period covered by this quarterly report, that ensure that information relating to the registrant which is required to be disclosed in this report is recorded, processed, summarized and reported, within required time periods. Based on this evaluation, our chief executive officer and chief financial officer have concluded that the registrant's disclosure controls and procedures were effective as of March 31, 2007.

There were no changes in the registrant's internal control over financial reporting during the period covered by this quarterly report that have materially affected, or are reasonably likely to materially affect the registrant's internal control over financial reporting.

## **Part II - Other Information**

### **Item 1. Legal Proceedings**

Verizon and a number of other telecommunications companies have been the subject of multiple class action suits concerning its alleged participation in intelligence-gathering activities allegedly carried out by the federal government, at the direction of the President of the United States, as part of the government's post-September 11 program to prevent terrorist attacks. Plaintiffs generally allege that Verizon has participated by permitting the government to gain access to the content of its subscribers' telephone calls and/or records concerning those calls and that such action violates federal and/or state constitutional and statutory law. Relief sought in the cases includes injunctive relief, attorneys' fees, and statutory and punitive damages. On August 9, 2006, the Judicial Panel on Multidistrict Litigation ( "Panel ") ordered that these actions be transferred, consolidated and coordinated in the U.S. District Court for the Northern District of California. The Panel subsequently ordered that a number of "tag along" actions also be transferred to the Northern District of California. Verizon has not answered or otherwise responded to any of the complaints. Verizon believes that these lawsuits are without merit.

*In the Matter of Certain Baseband Processor Chips and Chipsets, Transmitter and Receiver (Radio) Chips, Power Control Chips, and Products Containing Same, Including Cellular Telephone Handsets*, an action brought before the United States International Trade Commission (ITC), Broadcom Corporation alleges that certain chips and chipsets manufactured by respondent Qualcomm Corporation infringe three Broadcom patents. Broadcom is currently seeking a ban on the importation of certain devices containing Qualcomm's EV-DO chipsets, but not with respect to data cards, PDAs, smartphones or handheld email devices containing those chips. Verizon Wireless was granted permission to intervene in the proceeding on the issue of remedy but not on the issue of liability. The ITC staff, which is a party to the proceeding, has supported Broadcom's position with respect to liability and remedy. The trial on remedy was completed on July 11, 2006 before an ITC administrative law judge. The Administrative Law Judge issued an initial determination, finding that Qualcomm has infringed one of the three Broadcom patents and recommended that Qualcomm's chipsets should be excluded from importation into the United States. However, the Administrative Law Judge further recommended that Verizon Wireless handsets that incorporate the Qualcomm EV-DO chipsets should not be subject to an exclusion order. Broadcom and the ITC staff requested review of the initial determination by the full ITC. On December 8, 2006, the ITC affirmed in substantial part the Administrative Law Judge's initial determination with respect to liability, determining that Qualcomm infringed one Broadcom patent. The ITC held a public hearing on the issues of remedy and the public interest on March 21 and 22, 2007. The decision of the full ITC with respect to remedy is expected to be made by May 25, 2007. During a 60-day period following any exclusion order by the ITC, the President of the United States may disapprove the order. Further, ITC exclusion orders are reviewable by the U.S. Court of Appeals for the Federal Circuit. Disruption of the supply of handsets incorporating Qualcomm EV-DO chipsets could have a material adverse effect on the availability of handsets to sell to Verizon Wireless customers and could therefore have a material adverse effect on its business.

The New York State Department of Environmental Conservation has advised Verizon New York Inc. (VZNY) of potential issues in connection with its underground storage tank registration, inspection and maintenance program. While VZNY does not believe that any of the alleged conditions has resulted in a release or threatened release, aggregate penalties relating to alleged violations could exceed \$100,000 because of the number of tanks operated by VZNY. VZNY does not believe that the cost of remedying any alleged violations will be material.



**Table of Contents**

Verizon Wireless is conducting an audit of its cell site, switch and non-retail building facilities under an audit agreement with the U. S. Environmental Protection Agency. The first phase of the audit, covering approximately one-third of the facilities to be audited, identified potential violations of various laws governing hazardous substance reporting, air permitting and spill plan preparation. While Verizon Wireless does not believe that any of the alleged conditions has resulted in a release or threatened release, aggregate penalties relating to alleged violations could exceed \$100,000 because of the number of facilities operated by Verizon Wireless. Verizon Wireless does not believe that the penalties ultimately incurred and the cost of remedying any alleged violations will be material.

**Item 1A. Risk Factors**

Information related to our risk factors are disclosed under Item 1A to Part I of our Annual Report on Form 10-K for the year ended December 31, 2006.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following table provides information about Verizon's common stock repurchases during the first quarter of 2007:

| Period   | Total Number of Shares Purchased | Average Price Paid per Share | Maximum Number of Shares that  |  |
|----------|----------------------------------|------------------------------|--|--|
|          |                                  |                              | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | May Yet Be Purchased Under the Plans or Programs |
| January  | 2,900,000                        | \$ 37.37                     | 2,900,000  | 47,033,600                                       |
| February | 3,435,000                        | \$ 38.19                     | 3,435,000  | 43,598,600                                       |
| March    | 5,073,400                        | \$ 36.89                     | 5,073,400  | 95,479,000                                       |
|          | 11,408,400                       |                              | 11,408,400   | 95,479,000                                       |

On January 19, 2006, the Board of Directors approved a share buy back program which authorized the repurchase of up to 100 million common shares no later than the close of business on February 28, 2008. On March 1, 2007, the Board of Directors replaced the prior share buy back program with a new program for the repurchase of up to 100 million shares of Verizon common stock through the earlier of February 28, 2010 or when the total number of shares repurchased under the new buy back program aggregates to 100 million. The Board also determined that no additional shares were to be purchased under the prior program. Shares purchased on February 26 through 28, 2007 and settled in early March were authorized under the prior program. These programs permit Verizon to repurchase shares for the corporation over time, with the amount and timing of repurchases depending on market conditions and corporate needs. The Board also authorized Verizon to enter into Rule 10b5-1 plans from time to time to facilitate the repurchase of its shares. A Rule 10b5-1 plan permits the company to repurchase shares at times when it might otherwise be prevented from doing so, provided the plan is adopted when the company is not aware of material non-public information.

**Item 6. Exhibits**

(a) Exhibits:

**Exhibit Number**

- 10a Verizon Communications Inc. Long-Term Incentive Plan - Restricted Stock Unit Agreement 2007-09 Award Cycle.
- 10b Verizon Communications Inc. Long-Term Incentive Plan - Performance Stock Unit Agreement 2007-09 Award Cycle.
- 10c Verizon Communications Inc. Long-Term Incentive Plan - Special Restricted Stock Unit Agreement.

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- 10d Form of Addendum to Verizon Communications Inc. Long-Term Incentive Plan - Performance Stock Unit Agreement.
- 12 Computation of Ratio of Earnings to Fixed Charges.
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

**Table of Contents**

**Signature**

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Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: May 4, 2007

VERIZON COMMUNICATIONS INC.

By /s/ Thomas A. Bartlett  
Thomas A. Bartlett  
Senior Vice President and Controller  
(Principal Accounting Officer)

UNLESS OTHERWISE INDICATED, ALL INFORMATION IS AS OF MAY 3, 2007.