

# **Verizon North Inc.**

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Condensed Financial Statements  
Three and Six Months Ended June 30, 2008 and 2007

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Verizon North Inc.

CONDENSED STATEMENTS OF INCOME

(dollars in millions) (unaudited)	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
<b>Operating Revenues</b> (including \$291, \$292, \$577 and \$575 from affiliates)	\$ 801	\$ 824	\$ 1,587	\$ 1,641
<b>Operating Expenses</b> (including \$109, \$109, \$207 and \$220 to affiliates)				
Cost of services and sales (exclusive of items shown below)	167	175	344	354
Selling, general and administrative expense	139	137	251	281
Depreciation and amortization expense	265	266	522	532
<b>Total Operating Expenses</b>	571	578	1,117	1,167
<b>Operating Income</b>	230	246	470	474
Other income and (expense), net (including \$---, \$1, \$--- and \$1 from affiliates)	1	1	2	3
Interest expense (including \$(8), \$(8), \$(16) and \$(16) from affiliates)	(23)	(23)	(46)	(46)
<b>Income Before Provision for Income Taxes</b>	208	224	426	431
Provision for income taxes	(69)	(85)	(153)	(164)
<b>Net Income</b>	\$ 139	\$ 139	\$ 273	\$ 267

See Notes to Condensed Financial Statements

Verizon North Inc.

CONDENSED BALANCE SHEETS

(dollars in millions) (unaudited)	At June 30, 2008	At December 31, 2007
<b>Assets</b>		
Current assets		
Short-term investments	\$ 79	\$ 128
Accounts receivable:		
Trade and other, net of allowances for uncollectibles of \$28 and \$28	248	261
Affiliates	204	176
Materials and supplies	18	12
Prepaid expenses	12	19
Deferred income taxes	5	5
Deferred charges and other	51	61
Total current assets	<u>617</u>	<u>662</u>
Plant, property and equipment	11,297	11,211
Less accumulated depreciation	<u>8,333</u>	<u>8,160</u>
	<u>2,964</u>	<u>3,051</u>
Intangible assets, net	1,974	2,091
Prepaid pension asset	2,473	2,403
Other assets	36	42
Total assets	<u>\$ 8,064</u>	<u>\$ 8,249</u>
<b>Liabilities and Shareowner's Investment</b>		
Current liabilities		
Debt maturing within one year:		
Notes payable to affiliate	\$ 1,179	\$ 881
Other	501	502
Accounts payable and accrued liabilities:		
Affiliates	375	202
Other	185	215
Other current liabilities	180	211
Total current liabilities	<u>2,420</u>	<u>2,011</u>
Long-term debt	396	395
Employee benefit obligations	971	968
Deferred credits and other liabilities		
Deferred income taxes	1,705	1,779
Other	104	122
	<u>1,809</u>	<u>1,901</u>
Shareowner's investment		
Common stock (one share, without par value)	978	978
Contributed capital	1,041	1,041
Reinvested earnings	449	955
Total shareowner's investment	<u>2,468</u>	<u>2,974</u>
Total liabilities and shareowner's investment	<u>\$ 8,064</u>	<u>\$ 8,249</u>

See Notes to Condensed Financial Statements

**Verizon North Inc.**

**CONDENSED STATEMENTS OF CASH FLOWS**

(dollars in millions) (unaudited)	<b>Six Months Ended June 30,</b>	
	<b>2008</b>	<b>2007</b>
<b>Net Cash Provided by Operating Activities</b>	\$ 750	\$ 679
<b>Cash Flows from Investing Activities</b>		
Capital expenditures (including capitalized software)	(143)	(144)
Purchase of non-network software from affiliates	(175)	(411)
Net change in short-term investments	49	48
Other, net	1	2
Net cash used in investing activities	(268)	(505)
<b>Cash Flows from Financing Activities</b>		
Principle repayment of borrowings and capital lease obligations	(1)	(1)
Net change in notes payable to affiliates	298	154
Dividends paid	(779)	(325)
Net change in outstanding checks drawn on controlled disbursement accounts	---	(2)
Net cash used in financing activities	(482)	(174)
Net change in cash	---	---
Cash, beginning of period	---	---
Cash, end of period	\$ ---	\$ ---

See Notes to Condensed Financial Statements

**Verizon North Inc.**

**NOTES TO CONDENSED FINANCIAL STATEMENTS (Unaudited)**

**1. Basis of Presentation and Recent Accounting Pronouncements**

Verizon North Inc. (Verizon North or the Company) is a wholly owned subsidiary of GTE Corporation (GTE), which is a wholly owned subsidiary of Verizon Communications Inc. (Verizon). The accompanying unaudited condensed financial statements have been prepared in accordance with generally accepted accounting principles for interim periods. These condensed financial statements reflect all adjustments that are necessary for a fair presentation of results of operations and financial position 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. The condensed balance sheet at December 31, 2007 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. For a more complete discussion of significant accounting policies and certain other information, you should refer to our December 31, 2007 audited financial statements.

In April 2008, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) No. FAS 142-3, *Determination of the Useful Life of Intangible Assets* (FSP 142-3). FSP 142-3 removes the requirement under Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets* to consider whether an intangible asset can be renewed without substantial cost or material modifications to the existing terms and conditions, and replaces it with a requirement that an entity consider its own historical experience in renewing similar arrangements, or a consideration of market participant assumptions in the absence of historical experience. FSP 142-3 also requires entities to disclose information that enables users of financial statements to assess the extent to which the expected future cash flows associated with the asset are affected by the entity's intent and/or ability to renew or extend the arrangement. We are required to adopt FSP 142-3 effective January 1, 2009 on a prospective basis. We are evaluating the impact FSP 142-3 will have on our financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133*, (SFAS No. 161). This statement requires additional disclosures for derivative instruments and hedging activities that include how and why an entity uses derivatives, how these instruments and the related hedged items are accounted for under SFAS No. 133 and related interpretations, and how derivative instruments and related hedged items affect the entity's financial position, results of operations and cash flows. SFAS No. 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008.

In December 2007, the FASB issued SFAS No. 141(R), *Business Combinations (Revised)*, (SFAS No. 141(R)), to replace SFAS No. 141, *Business Combinations*. SFAS No. 141(R) requires the use of the acquisition method of accounting, defines the acquirer, establishes the acquisition date and broadens the scope to all transactions and other events in which one entity obtains control over one or more other businesses. This statement is effective for business combinations or transactions entered into for fiscal years beginning on or after December 15, 2008. The adoption of this statement will not have any impact to our financial statements.

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51*, (SFAS No. 160). SFAS No. 160 establishes accounting and reporting standards for the noncontrolling interest in a subsidiary and for the retained interest and gain or loss when a subsidiary is deconsolidated. This statement is effective for financial statements issued for fiscal years beginning on or after December 15, 2008. The adoption of this statement will not have any impact to our financial statements.

**2. Shareowner's Investment**

(dollars in millions)	Common Stock	Contributed Capital	Reinvested Earnings
Balance at December 31, 2007	\$ 978	\$ 1,041	\$ 955
Net income	---	---	273
Dividends paid	---	---	(779)
Balance at June 30, 2008	\$ 978	\$ 1,041	\$449

Net income and comprehensive income were the same for the three and six months ended June 30, 2008 and 2007, respectively.

### 3. Fair Value Measurements

#### *SFAS No. 157*

SFAS No. 157, *Fair Value Measurements* (SFAS No. 157) defines fair value, establishes a framework for measuring fair value and establishes a hierarchy that categorizes and prioritizes the sources to be used to estimate fair value. SFAS No. 157 also expands financial statement disclosures about fair value measurements. On February 12, 2008, the FASB issued FSP No. FAS 157-2 (FSP 157-2), which delays the effective date of SFAS No. 157 for one year for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis. We elected a partial deferral of SFAS No. 157 under the provisions of FSP 157-2 related to the measurement of fair value used when evaluating intangible assets and other long-lived assets for impairment and valuing asset retirement obligations and liabilities for exit or disposal activities. Furthermore, the impact of implementing FSP 157-2 is not expected to be material to our financial statements. The impact of partially adopting SFAS No. 157 effective January 1, 2008 was not material to our financial statements.

#### *Fair Value Measurements on a Recurring Basis*

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurements. Our assessment of the significance of a particular input to the fair value measurements requires judgment, and may affect the valuation of the assets and liabilities being measured and their placement within the fair value hierarchy.

The following table presents the asset balances measured at fair value on a recurring basis as of June 30, 2008:

(dollars in millions)	Level 1 <sup>(1)</sup>	Level 2 <sup>(2)</sup>	Level 3 <sup>(3)</sup>	Total
Assets:				
Short-term investments	\$ —	\$ 79	\$ —	\$ 79

<sup>(1)</sup> – quoted prices in active markets for identical assets or liabilities

<sup>(2)</sup> – observable inputs other than quoted prices in active markets for identical assets and liabilities

<sup>(3)</sup> – no observable pricing inputs in the market

Short-term investments primarily include a fund comprised of cash equivalents held in trust for the payment of certain employee benefits and are classified as Level 2 as they are not actively traded in an established market. The decrease in our short-term investments during the six months ended June 30, 2008 was due to the payment of these employee benefits.

#### *Fair Value Measurements on a Nonrecurring Basis*

As permitted by FSP 157-2, we elected to defer the fair value measurement disclosure of our (a) long-lived assets and finite life intangible assets in the determination of impairment under SFAS No. 142 or SFAS No. 144, (b) asset retirement obligations initially measured at fair value under SFAS No. 143 *Accounting for Asset Retirement Obligations*, and (c) nonfinancial liabilities for exit or disposal activities initially measured at fair value under SFAS No. 146 *Accounting for Costs Associated with Exit or Disposal Activities*.

#### *SFAS No. 159*

SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of SFAS No. 115* (SFAS No. 159), permits but does not require us 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. As we did not elect to fair value any of our financial instruments under the provisions of SFAS No. 159, our adoption of this statement effective January 1, 2008 did not have an impact on our financial statements.

**4. Commitments and Contingencies**

Various legal actions and regulatory proceedings are 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 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 will have a material effect on our financial condition, but it could have a material effect on our results of operations.

From time to time, state regulatory decisions require us to assure customers that we will provide a level of service performance that falls within prescribed parameters. There are penalties associated with failing to meet those service parameters and we, from time to time, pay such penalties. We do not expect these penalties to have a material effect on our financial condition, but they could have a material effect on our results of operations.

**5. Subsequent Events**

On August 1, 2008, we declared and paid a dividend in the amount of \$476 million to our parent, GTE.