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October 31, 2001

**VIA FEDERAL EXPRESS**

Mr. Thomas M. Dorman  
Executive Director  
Commonwealth of Kentucky  
Public Service Commission  
211 Sower Boulevard  
Frankfort, KY 40602

RECEIVED

OCT 01 2001

FEDERAL EXPRESS  
DORMAN, THOMAS M.

**Re: Information filing of Talk America, Inc. and The Other Phone Company, Inc. d/b/a Access One Regarding Their Intent to Guarantee and Provide Other Security in Connection with Financing Transactions of Their Parent, Talk America Holdings, Inc.**

Dear Mr. Dorman:

TALK AMERICA, INC. ("Talk America") and THE OTHER PHONE COMPANY, INC. D/B/A ACCESS ONE ("TOPC") (collectively, the "Talk Subsidiaries" or "Parties"), by their attorneys, hereby respectfully advise the Kentucky Public Service Commission ("Commission") of their intent to provide their guarantee and to provide other security in connection with financing transactions being arranged for their parent, Talk America Holdings, Inc. ("Talk Holdings"). In Kentucky, Talk America is authorized to provide competitive local telecommunications services,<sup>1</sup> and TOPC is authorized to provide competitive local and interexchange telecommunications services.<sup>2</sup> Pursuant to the exemptions set forth in Administrative Case Nos. 359 and 370, the Parties believe that no approval by this Commission is required in connection

<sup>1</sup> No. 61-1511 dated 6/4/01 (initially certified as Tel-Save on 11/2/96), CLEC ID#5051890.

<sup>2</sup> CLEC ID#5010600 dated 7/9/98; IXC ID#22250106 dated 9/18/99.

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with this transaction. In support of this notification, the Parties provide the following information:

**The Company.** Talk America is a direct, wholly owned subsidiary of Talk Holdings. TOPC is an indirect, wholly owned subsidiary of Talk Holdings. Talk Holdings is a publicly held Delaware corporation with principal offices at 12020 Sunrise Valley Drive, Suite 250, Reston, Virginia 20190. Through its subsidiaries, Talk Holdings provides a suite of intrastate local and/or long distance telecommunications services to business and residential customers virtually nationwide via resale or the use of UNE-Platform arrangements where available. Talk America also is authorized by the FCC to provide interstate and international telecommunications services.

**The Transaction.** This transaction involves the restructuring of Talk Holdings' obligations to America Online, Inc. ("AOL") that originally arose under the Investment Agreement that the parties entered into on January 5, 1999 when AOL purchased 4,121,372 shares of Talk Holdings' common stock from Talk Holdings. Pursuant to a Restructuring and Note Agreement, dated as of September 19, 2001 (the "Restructuring Agreement"), between Talk Holdings and AOL, Talk Holdings issued \$54 million principal amount of its 8% Secured Convertible Notes due 2011 (the "Convertible Notes") in exchange for a release of Talk Holdings' obligations under the Investment Agreement to reimburse AOL for losses AOL might incur on the sale of Talk Holdings' shares that it acquired in January 1999.<sup>3</sup> Effective October 1, 2001, in connection with the termination of a marketing arrangement between Talk America and AOL, the aggregate principal amount of the Convertible Notes was reduced to approximately \$34.1 million.

The Convertible Notes are convertible at any time into shares of Talk Holdings' common stock at an initial conversion price of \$5.00 per share, may be redeemed by Talk Holdings at any time without premium and are subject to mandatory redemption at the option of the holder on the fifth and seventh anniversaries of their issue date.<sup>4</sup> Talk Holdings may also elect to pay up to 50% (100% in the case of the first interest payment) of the interest on the Convertible Notes in kind rather than in cash. The Convertible Notes are secured by a pledge of all of Talk Holdings' assets.<sup>5</sup> Although no regulatory approval is required for Talk Holdings to effect the restructuring or to issue the Convertible Notes because it is not itself a utility, in some states, not including

<sup>3</sup> As part of the transaction, AOL surrendered for cancellation warrants it held to acquire additional stock of Talk Holdings in return for an additional 3.1 million shares of Talk Holdings' common stock that, together with the 4.1 million shares previously acquired, represent less than 10% of the outstanding common stock of Talk Holdings.

<sup>4</sup> Of course, in the event AOL elects to exercise its conversion rights, any necessary regulatory approvals will be sought prior to the issuance of additional common stock.

<sup>5</sup> The stock of the subsidiaries of Talk Holdings, including that of the Parties, is also being pledged to AOL as security for the Convertible Notes.

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Kentucky, approval is required for the Talk Subsidiaries to assume certain obligations with respect to the Convertible Notes.

As a condition to this transaction, certain subsidiaries of Talk Holdings, including the Talk Subsidiaries, have executed a Master Subsidiary Guarantee, Security Agreement, Collateral Assignment and Equity Pledge dated September 19, 2001 in favor of State Street Bank and Trust Company, N.A., as collateral agent for AOL (the "Subsidiaries' Agreement"). Pursuant to the Subsidiaries' Agreement, such subsidiaries have guaranteed Talk Holdings' obligations under the Convertible Notes and have pledged all of their respective assets to secure Talk Holdings' obligations under the Convertible Notes, in each case including any additional notes issued in lieu of cash interest.

The security documents contain appropriate provisions indicating that the exercise by AOL of certain rights thereunder (for example, effecting a change in the direct or indirect ownership or control of regulated subsidiaries) are subject to obtaining prior regulatory approval. Most importantly, the Subsidiaries' Agreement provides that neither the guarantee of the Talk Subsidiaries nor the security interest in their respective assets will become effective until all necessary regulatory approvals have been obtained.

**Public Interest Considerations.** This financing transaction will serve the public interest by enhancing the ability of the company to grow and compete in the highly competitive markets for telecommunications services in Kentucky and nationwide. The transaction will enable the company to avoid substantial financial obligations and instead devote its financial resources to develop new products and services and respond to the highly competitive telecommunications environment. This transaction is not expected to affect in any way Talk America's or TOPC's current rates or services in Kentucky or elsewhere.

In addition, because of the highly competitive environment in which it operates, the rates charged customers are subject to market discipline and the services offered are generally available from other carriers. As a result, the source of funds and capital structure of Talk Holdings and the provision of guarantees and security interests in assets by the Talk Subsidiaries would have little effect on customers in Kentucky or elsewhere. In the unlikely event that the companies' capital structure or obligations become too costly and rates rise to compensate, customers may simply migrate to other carriers with preferred rates. Thus, any adverse consequences from the companies' financing decisions impact primarily on shareholders, not on the companies' customers, and any favorable consequences benefit both shareholders and consumers through higher profits, lower rates and better services. Finally, the Parties note that Talk Holdings, a publicly held company, is subject to the jurisdiction of the Securities and Exchange Commission. This also serves to protect the interests of the companies' investors and customers in Kentucky.

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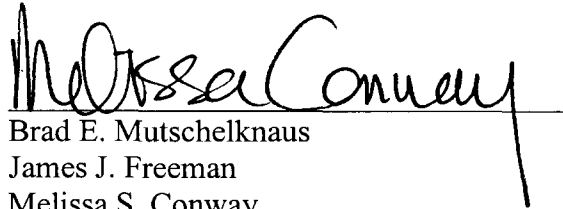
As noted above, it is the Parties' understanding that prior Commission approval is not required to consummate the transaction described herein. This information is being submitted, therefore, solely to keep the Commission advised and its records current.

Enclosed please find ten (10) copies and a duplicate copy of this filing. Also enclosed is a self-addressed, postage-paid envelope. Please date-stamp the duplicate upon receipt and return it in the envelope provided. Please do not hesitate to contact Melissa Conway at (202) 955-9667 if you have any questions.

Respectfully submitted,

TALK AMERICA, INC.  
THE OTHER PHONE COMPANY, INC. D/B/A ACCESS  
ONE

By:



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James J. Freeman  
Melissa S. Conway  
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Its Attorneys

**VERIFICATION**

I, Aloysius T. Lawn IV, am authorized to represent Talk America Holdings, Inc. and its subsidiaries and to make this verification on their behalf. Except as otherwise specifically attributed, the statements in the foregoing document relating to these companies are true of my own knowledge, other than as to matters that are stated therein on information on belief, and as to those matters, I believe them to be true. I declare under penalty of perjury that the foregoing is true and correct.

Aloysius T. Lawn IV

Aloysius T. Lawn IV  
Executive Vice President - General Counsel  
and Secretary  
Talk America Holdings, Inc.

Subscribed and sworn to before me this 18<sup>th</sup> day of October, 2001.

Amy McCusker  
Notary Public

My Commission expires: 4/27/04

