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March 14, 2001

To All Creditors and Holders of Payphone
Leases With ETS Payphones, Inc.

Re: Chapter 11 Bankruptcy Cases of
ETS Payphones, Inc. et al.

Dear Sir or Madam:

This firm is counsel for the Official Committee of Unsecured Creditors (the "Committee") of ETS Payphones and its affiliated chapter 11 debtors (collectively, "ETS" or the "Debtors"). We are writing on behalf of the Committee to provide you with an informational update, including progress and developments made in the case to date, the status of ETS' operations, and the Committee's general direction and goals in these cases. For your information, three of the five members of the Committee are leaseholders.

As a preliminary matter, we know that many leaseholders have been frustrated by ETS' inability since the beginning of these cases to continue monthly payments. In addition, we are aware that leaseholders and others may desire easier and more frequent access to reliable public information concerning this case. As you may recall, last fall we sent an introductory letter to all leaseholders. Since that time, as you will see below, the Committee has been extremely active, and the case has been in a state of flux. As a result, update letters would not have been meaningful for you because information was constantly being obtained, evaluated, modified or quickly outdated. Nevertheless, the practical difficulty of disseminating accurate and meaningful information has apparently led to the circulation among many leaseholders and creditors of an abundance of rumors and inaccurate or mischaracterized information, or has otherwise created other concerns among leaseholders. We hope that this letter and further updates will help to remedy this situation and will be responsive to your questions and concerns.

Management Issues And The New CEO

During the opening weeks of the case, the Committee endeavored to review the operations of ETS and the prospects for achieving an effective reorganization. Unfortunately, the Committee encountered a variety of difficulties, particularly in the area of obtaining accurate or reliable information from ETS. The Committee grew increasingly concerned with the effectiveness of management, as well as with the operational performance of the payphones. This ultimately led to the Committee's December 19, 2000 motion (which, in non-legalese, is a request) to the Bankruptcy Court for the appointment of a Chapter 11 trustee to replace management. Litigation against ETS ensued.

To avoid the expense, delay and risk associated with continuing this litigation, ETS and the Committee entered into a settlement agreement. This settlement was approved by the Court, and provided for the appointment of a new Chief Executive Officer to be selected by ETS from a list of qualified and acceptable candidates suggested by the Committee. In mid-January, 2001, the Committee interviewed 10 people (selected from a broader field) and identified a slate of three acceptable candidates. ETS then interviewed the candidates and selected Guy Longobardo as the new CEO.

Mr. Longobardo's background is diverse and appropriately tailored to the needs of this case. He was a *cum laude* graduate of Williams College and a Harlan Fiske Stone Scholar at Columbia University School of Law. He then began his career as a corporate lawyer with the prestigious law firm of Milbank Tweed Hadley & McCloy in New York, and he later became an investment banker with HSBC, rising to the level of Managing Director and the Head of Corporate Finance. He left HSBC to became an executive with AMNEX, Inc. and its affiliated telecommunications companies that were experiencing financial difficulty and required new management. Although Amnex itself ended up in chapter 11, Mr. Longobardo's efforts were respected, including his assistance in operating its 11,000 payphone subsidiary during a time of crisis, and in carrying out the sale of such payphones (at the express urging of that company's creditors) for $24.9 million. Because of the numerous issues and matters that need to be addressed in ETS' case -- complex issues of bankruptcy law, securities law, finance, fraud and telecommunications are implicated in addition to the task of operating the payphones -- the Committee believes that Mr. Longobardo's broad-base of experience, ability and integrity will be invaluable in guiding ETS through the reorganization process.

The Committee also believes that although Mr. Longobardo's compensation, agreed to after strenuous negotiations with the Debtor, may be viewed by some as relatively high, it is not inconsistent with what was requested by other candidates or with the "market" for executives of companies of ETS' size and condition. In addition, he is appropriately incentivized to achieve favorable results for leaseholders. His compensation package consists of a base salary of $30,000 per month, and an opportunity to receive a bonus in an amount that is tied to the performance of ETS (and thus the returns to leaseholders) as well as the date that ETS effectuates a plan of reorganization. In agreeing to this compensation package, the Committee recognized that the position of new CEO will be extremely demanding and that only a limited number of people were willing, able and qualified to take the job. Moreover, other suitable crisis managers required in excess of $50,000 per month, plus unquantified incentive bonuses.

Mr. Longobardo began work full-time on February 26, 2001, only 16 days ago. The Committee hopes and expects that Mr. Longobardo will expeditiously and incisively review ETS' operations at every level for the reasons described below. He is also expected to formulate a proposal for reorganizing ETS, with the advice and input of the Committee. These matters are expected to occur in the next 30-60 days.

<u>Financial Performance and Projections</u>

Since its appointment, the Committee has learned a number of things about ETS' pre-bankruptcy financial performance. Most significantly, ETS' payphone operation by itself (i.e. excluding the proceeds from sales of payphones to leaseholders), was losing money at the rate of over $66 million per year, despite statements or representations made to you by others. The monthly payments to investors were possible only because of the cash generated by sales of payphones to new investors. (The term "investor" is used interchangeably with "leaseholder" in this letter, reflecting different terms used by the general body of investors/leaseholders.) This scheme of using new investors' money to pay obligations to existing investors led the SEC to refer to this enterprise as a "ponzi scheme". Moreover, it bolsters the notion that ETS' payphone operations were not particularly well-run, since ETS presumably would have been more concerned with generating cash from sales of payphones to new investors than it was with ensuring that payphone operations were profitable.

Additionally, other industry-wide factors clearly have depressed and continue to depress the financial performance of ETS. These factors include the increased usage of cellular telephones, increased usage of dial-around services (such as 1-800-CALL-ATT), and site owners' demands for increasing commissions.

From the beginning of this case, the ultimate goal has been to "turn around" ETS' payphone operations so that profits and any excess cash could be distributed to leaseholders and other creditors. In order to measure the performance of ETS, like that of any company, it is necessary to have accurate and reliable accounting and appropriate financial controls. ETS had never been required to report to the public or to make projections, and its accounting methods were sorely deficient. It appears that with the assistance of an outside accounting firm and a new Chief Financial Officer hired in mid-December, 2000, ETS' financial reporting has improved significantly.

Unfortunately, along with the improvement in the accuracy and reliability of ETS' accounting has come an extremely troubling picture. In the opening weeks and months of this case, the Committee was advised and given the impression that ETS was operating on at least a break-even basis (without paying leaseholders), and that ETS could be expected to generate at least a few hundred thousand dollars a month in excess cash that could presumably be set aside and later paid to leaseholders and creditors. The president and then CEO of ETS, Mr. Jim Blyth, testified in December, 2000 that he believed it was reasonable to strive for up to $1 million per month in excess cash. All of these relatively favorable projections however, were done at a time when, it was later determined, ETS was not able to produce reliable financial reports or projections.

In late January, 2001, ETS provided the Committee with a new and more accurate set of financial reports and projections. These projections showed that ETS was actually losing substantial sums each month. In addition, if all operating expenses continued to be paid, ETS would literally run out of cash by the end of February, 2001.

This new set of operating results and projections clearly shocked the Committee. We reviewed them with ETS and its professionals (including the outside accounting firm), and we have determined that, unfortunately, they appear to be reasonably accurate.

<u>ETS' Actions To Attempt A Turnaround</u>

Facing the prospect of running out of cash, ETS took action to further reduce its expenditures. In light of a recent audit that showed ETS had overpaid certain commissions to site owners, ETS temporarily stopped paying commissions. Although this move carried with it the risk that ETS may lose site locations, ETS simply had no choice, and in any event it has enabled ETS to perform a more complete audit of its commission payment procedures. The Debtors expect to resume paying commissions in April 2001.

Even with the moratorium on commission payments, the Debtors' current projections reflect that the Debtors will run out of cash by the end of June, 2001. A summary of the Debtors' operating results and projections is provided at the conclusion of this letter.

The new CEO is being asked to address this issue with priority, and to determine whether there are any steps that could be taken to avoid the significant interruption or termination of ETS' operations. The Committee understands that many cost-cutting measures were previously implemented by former CEO Jim Blyth. These measures included switching the dial-tone service provider from Local Exchange Carriers (such as Verizon or Bell South) to Competitive Local Exchange Carriers (such as North American Telecommunications Corp.) in order to receive somewhat lower rates. Similarly, numerous employees' jobs were terminated, and approximately 6,000 unprofitable phones (i.e., phones whose annual revenues are less than their direct expenses) were disconnected and removed from their site locations.

It is now up to the new CEO to determine if additional cost saving (or revenue enhancing) measures are possible and whether they will result in an effective turnaround. We understand that the new CEO has already scheduled another 7,800 unprofitable phone lines to be disconnected, and that this move should save roughly $1 million over the course of the next year. In addition, certain security and other measures are being implemented that may result in increased coin collection. But these steps are not likely to be enough to overcome ETS' cash flow deficiencies, and we anticipate additional efforts will be forthcoming.

In the event that the payphone operations remain unprofitable, the Committee expects that there may be two potential methods for leaseholders and creditors to realize some value from ETS' business. The first method would be to turn over the management of the payphones to another company. Such a management arrangement may require ETS to pay monthly fees, but ETS would no longer be required to pay for the maintenance of the phones or for substantially all of its overhead. From ETS' perspective, the net benefits of a management arrangement would depend primarily upon both the amount of monthly fees required and the ability of the manager to raise revenue from the payphones. In this age of declining revenues and challenges facing the payphone business, it would be no small task to find an appropriate and qualified manager.

The second method of realizing value if ETS' operations cannot be salvaged would be to sell ETS' business as a going concern and thereafter distribute the proceeds to leaseholders and creditors. There are many hurdles associated with any such sale. First, it is unclear whether ETS would have the requisite authority or title to convey the payphones to a buyer. This sale, therefore, would in all likelihood require the support of leaseholders. Second, in light of the declining market for payphones, it is likely to be difficult to find a buyer. This would especially be the case if ETS sought to sell all of the payphones, as opposed to only the payphones located in specific geographic areas. Third, it may be difficult to obtain a purchase price paid wholly in cash, since the depressed payphone market may make it difficult for any buyer to obtain financing for the purchase price. To the extent any of the purchase price were to be paid with a promissory note or stock, the value of such note or stock would be almost entirely dependant on the identity, qualifications and abilities of the buyer.

Clearly, therefore, ETS, its leaseholders and creditors are in an enormously difficult situation. The work of the new CEO over the next few weeks will be crucial to determining the outcome of this case, and the Committee will be monitoring all developments.

The Leaseholders' Rights Under the Bankruptcy Code

At this point, leaseholders are undoubtedly wondering "but how does ETS' attempted turnaround and business plan affect me? When will I get paid? What are my rights?" To answer these questions, we must first provide a description of how the Bankruptcy Code would treat the payphone leases.

The Bankruptcy Code requires a debtor such as ETS either to "assume" or "reject" leases and certain contracts prior to confirmation of a plan of reorganization and the debtor's exit from chapter 11. Assumption of a lease means, in essence, the affirmance of the debtor's rights and obligations under the lease, and the debtor's continuation of the use of the leased property. Rejection of the lease means that the debtor no longer wants or needs the leased property, and such property is returned to the lessor or property owner.

In order for a debtor to "assume" a lease, the debtor must (a) cure all monetary defaults and (b) provide adequate assurance of future performance under the lease. In other words, to assume a lease the debtor must pay all amounts that have come due under the lease, and the debtor must further show that it has the financial wherewithal to pay amounts due under the lease in the future.

ETS clearly cannot assume the payphone leases. The monthly payment obligations under the leases amounted to approximately $5 million per month, and roughly $30 million has accrued since September, 2000. As described above, ETS simply does not have any excess cash, much less anything close to the required $30 million. Moreover, as demonstrated by the results of operations and the projections, ETS could not possibly show that it can resume $5 million in monthly payments to leaseholders. Consequently, assumption of the leases is not a realistic possibility.

Rejection of the leases may at first sound attractive (for those who say "I want my phones back"), but in fact it would be a financial disaster for leaseholders and would further result in an inequitable distribution among leaseholders. The documents state that leaseholders own only the payphone equipment, not the location in which the payphone may have been installed. Rejection of the payphone leases, therefore, would only require ETS to remove the payphones from their locations and return the equipment to leaseholders.

The used payphones would have little or no value to leaseholders. Each unit of used payphone equipment is currently worth only about $100, subject to small variations based upon the type and condition of the payphone equipment. A leaseholder is likely to have difficulty selling a unit of payphone equipment, since (a) the payphone market in general is in steep decline, (b) ETS' rejection of leases would flood the market with roughly 50,000 used payphones, and (c) the largest manufacturer of new payphones, Elcotel, is itself in bankruptcy and could be expected to sell off significant portions of its inventory of new equipment. Rejection of the payphone leases, therefore, would not only destroy whatever enterprise value ETS has, but in all likelihood would provide no meaningful financial recovery for leaseholders.

Rejection of the payphone leases would also provide absolutely no return to those investors who were unfortunate enough to have put up their money in the few months immediately leading up to the bankruptcy filing. For many, if not all of these people, there may be in fact no piece of payphone equipment in ETS' possession. Thus, even though the funds from these relatively new investors were used to pay existing investors, rejection of the payphone leases would result in no benefit to the new investors.

Even some of the existing leaseholders may not receive any benefit from rejection of the leases. The Committee understands that many payphones (the exact number is unclear, but it runs into the thousands) were used, or "cannibalized" for spare parts to repair other installed payphones. Clearly, the return of a cannibalized piece of equipment would have no benefit to a leaseholder.

Since the payphone leases can neither be assumed nor rejected, what can be done for the leaseholders? The Committee believes that the only option is for an accommodation to be reached that would enable all leaseholders to realize the maximum possible value of ETS' payphone business as a going concern -- whatever value that may be -- and for the leaseholders to share such value amongst themselves in an equitable, *pro rata*, fashion.

Plan Structure -- *Pro Rata* Distributions To Leaseholders

The value of ETS' business as a going concern rests primarily in the locations of the payphones and the operations of the business. The few payphones that are located in high-traffic areas have greater usage (and more revenue) and in certain areas may even have the potential for generating advertising revenue. Payphones in other locations are either unlikely to generate a meaningful profit (i.e. value to the leaseholders), or can generate value only with constant attention and vigilant management. The task for the new CEO and ETS, which is urgently being addressed, is to maximize and harness the value of this payphone business.

As previously described, the value of ETS possibly can be realized from a turnaround of ETS' operations, a management arrangement with a third party, the sale of payphone routes, or some combination of these options. In the end, the Committee is hopeful that there may either be some positive cash flow each month, which would arise from a turnaround of operations or a management arrangement, or there will be proceeds from a sale or other transaction involving another sizeable payphone operator. In either case, the leaseholders will have to determine how such value should be allocated among them.

The Committee is of the view that leaseholders should be treated equally without regard to the particular locations of the leased payphone equipment. For example, if two leaseholders invested $7,000 each (representing one phone) on the same day, and one of the leased phones has been disconnected while the other leased phone generates profit, should the two leaseholders receive a different share of the distributions in this case? The Committee thinks not, and believes instead that these two leaseholders should share equally in any distributions.

In reaching this conclusion, the Committee recognizes that the leaseholders had essentially no control over selecting the location of leased phones. Thus there is no logical basis on which to favor the few leaseholders who by sheer luck have well-situated phones, while punishing those who were unlucky enough to have poorly located phones. Accordingly, the Committee believes that recoveries should be shared by all leaseholders on a *pro rata* basis, based upon the amount of money each leaseholder has invested.

In order to implement this equitable distribution concept, however, it is necessary essentially to "re-write" the otherwise operative documents between the leaseholders and ETS in a fully uniform fashion. Such a uniform revision to the documents can only be achieved by Court order, so that none of the leaseholders who may have leased relatively valuable phones seek to remove such phones from the entire "pool" of phones, to the extreme detriment of other leaseholders.

The exact nature of such a Court order is currently a topic of discussion between the Committee and ETS. One form of order suggested by ETS would be entered as part of a class action involving all leaseholders. As envisioned by ETS, the class action would not actually be litigated by the parties, but would instead be settled in a manner that would implement both the equitable distribution concept described above as well as the business plan and plan of reorganization to be discussed with the Committee. The Committee will clearly need to investigate this proposed mechanism to ensure that leaseholders' rights and interests are protected. The Committee takes the view, however, that so long as the end result has the support of leaseholders and with all factors considered is in the best interests of leaseholders, the legal methodology used to achieve the result has little practical importance.

Conclusion

The Committee also anticipates that leaseholders and creditors may have questions or concerns about matters that are unrelated to the substance of this letter. We have tried to address some of such questions in the attached "Answers to Frequently Asked Questions." Please feel free to contact us with your additional questions. Such questions should be in writing, however, as it is easier for us to track our responses to written communications (and please include your e-mail address, if any, so that we can keep costs down). We will also continue to keep you apprised of developments, through either further written updates or our dedicated phone line (212-940-6777).

Although the Committee recognizes that there are challenging hurdles and decisions ahead, the Committee will continue to work towards ensuring that the most favorable result possible will be achieved. The Committee hopes that it has your continuing support to carry out its duty in this case.

In re ETS Payphones, Inc. et al.
Attachment to March 14, 2001 Letter to Leaseholders

(000's)	Actual Results					Forecast			
Description	October	November	December	January	February	March	April	May	June
Receipts (includes coin, operator services, dial around, etc.)	7,643 (includes dial around)	4,239 (includes extra-ordinary items)	4,122 (includes extra-ordinary items)	7,050 (includes dial around)	3,215	3,855	6,656 (includes dial around)	3,827	3,987
Disbursements									
Direct (includes LEC, commissions, taxes, etc.)	4,250	5,068	4,716	3,731 (nearly all commissions unpaid)	3,182 (nearly all commissions unpaid)	3,535 (nearly all commissions unpaid)	4,254	5,059	3,940
Overhead (includes payroll, chapter 11 expenses, taxes, etc.)	884	903	1,158	1,019	1,027	1,103	1,163	1,517	1,273
ATM Cash	161	25	281	0	(111)	0	0	0	0
Total Disbursements	5,295	5,996	6,115	4,750	4,098	4,638	5,417	6,576	5,213
Total Receipts over (under) disbursements	2,348	(1,757)	(2,033)	2,300	(883)	(783)	1,239	(2,749)	(1,226)
Forecasted beginning cash balance						2,491	1,708	2,947	198
Forecasted ending cash balance						1,708	2,947	198	(1,028)

In re ETS Payphones, Inc.
Attachment to March 14, 2001 Letter to Leaseholders

Answers To Frequently Asked Questions

Q: *What happened to Charles Edwards and his assets?*

A: Charles Edwards' assets and those of his wholly-owned company Twinleaf, Inc. are still frozen by order of the U.S. District Court in Atlanta. The Committee conducted a deposition of Mr. Edwards in late January and attended another deposition conducted by the receiver for Phoenix Telecom. The Committee has also been in regular contact with the SEC concerning the claims against Mr. Edwards. The Committee expects a substantial recovery from Mr. Edwards and Twinleaf, through further litigation or settlement. However, given the sheer magnitude of leaseholders' investments (over $350 million in the aggregate), the Committee also recognizes that a recovery from Mr. Edwards is not likely to have a material effect on the ultimate return to leaseholders.

Q: *When and how do I file a proof of claim?*

A: A form of proof of claim specifically to be used by all leaseholders has been prepared. The forms have been designed to be easy to read (i.e., no legalese) and are tailored to permit leaseholders to assert claims in a uniform fashion. The forms will be mailed out in the next few weeks, along with instructions and an indication of a deadline that should be about one month after the date you receive the form. Please make sure that you complete and file the claim form promptly upon your receipt, since the Bankruptcy Court will strictly observe the deadline.

Q: *What is the bottom line? How much money will I get back?*

A: Although this sounds like a simple and direct question, there can be no answer for all of the reasons described in the accompanying letter. Nevertheless, leaseholders should anticipate a substantial loss of the principal amount of their investment.

Q: *Isn't it true that lawyers are the only ones benefiting from this case?*

A: Although the Bankruptcy Code provides that lawyers retained by ETS and the Committee have administration expense claims that must be paid "off the top", the Bankruptcy Court has the ultimate authority to determine whether legal fees are reasonable. For our part, we believe that the time we have expended has been kept to a reasonable and necessary minimum but consistent with what was and is believed required in order to adequately and properly represent the interests of the Committee and, by extension, the leaseholders and creditors at large. Moreover, although it may be tempting for some to blame lawyers for the present set of circumstances, we respectfully ask that leaseholders and creditors bear in mind that we did not play any role in connection with ETS and its affiliated entities prior to the commencement of these cases.

Q: *Have you heard of Midwest Financial's Re-Start Program? Is it a good idea?*

A: The Committee is aware that an entity known as Midwest Financial ("Midwest") located in Michigan has offered (the "Offer") to take over leaseholders' phones and to resume monthly payments, in exchange for a fee. The Committee believes that an abundance of caution and prudence must be used in connection with considering and evaluating its solicitation and proposal. The Offer is not being made with the approval or cooperation of the Debtors or the Committee. It is unsolicited. Nor has the Offer been made in any fashion with the approval, or even the knowledge of the Bankruptcy Court. The Offer also appears to seek to make Midwest an assignee of the rights and interests of existing leaseholders. As such, Midwest would not have any better or greater rights with respect to the payphones than the leaseholders (see the description of assumption or rejection of leases in the accompanying letter). In addition, given the apparent lack of any financial information concerning Midwest, persons reviewing the Offer should be concerned with and evaluate Midwest's ability to make the payments it has promised. Moreover, its request for leaseholders to pay more money should be viewed with great caution. Furthermore, the Committee understands that Midwest has been or may be the subject of a cease and desist order in the State of California (as was ETS) and perhaps other jurisdictions, which raises questions about the nature of Midwest's business practices.

Q: *Have you heard of Mike Scott's web site and his offer to take over management of the payphones?*

A: The Committee is aware of the web site (www.payphoneoperators.org), and we have mixed feelings about it. On the one hand, the web site has been a somewhat positive development because it has served as a vehicle for certain leaseholders to express their frustration, and it has highlighted the need for increased communication between the Committee and the leaseholders in general. On the other hand, certain information in the web site appears to be misleading or erroneous. For example, the web site suggests that ETS should be able to return $30 to $60 per payphone per month to leaseholders, even though, as described in the accompanying letter, ETS is not cash flow positive and the entire payphone business is in a steep decline. In addition, the web site refers to taking over management of the payphones, but it is unclear precisely who would be designated to be in charge of ETS, or what the qualifications of such person are to operate payphones or to deal with the myriad issues present at ETS.