TALK AMERICA HOLDINGS INC
Form PREM14A
October 02, 2006

**UNITED STATES**
**SECURITIES AND EXCHANGE COMMISSION**
**WASHINGTON, D.C. 20549**

**SCHEDULE 14A**

**PROXY STATEMENT PURSUANT TO SECTION 14(a) OF THE SECURITIES EXCHANGE ACT OF 1934**

Filed by the Registrant X

Filed by a Party other than the Registrant ___

Check the appropriate box:

X Preliminary Proxy Statement

Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e) (2))

Definitive Proxy Statement

Definitive Additional Materials

Soliciting Material Pursuant to Rule 14a-11(c) or Rule 14a-12

**TALK AMERICA HOLDINGS, INC.**

(Name of Registrant as Specified In Its Charter)

N/A

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

No fee required.

X Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:
Common stock, par value $0.01 per share, of Talk America Holdings, Inc. ("Talk America")

(2) Aggregate number of securities to which transaction applies:
31,494,519 shares of Talk America common stock (including options to purchase 985,881shares of Talk America common stock)

(3)

Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

The filing fee of $26,854.30 was calculated pursuant to Exchange Act Rule 0-11(c) and was determined by multiplying 0.000107 by the sum of (i) the product of 30,508,638 shares of Talk America common stock outstanding and the merger consideration of $8.10 per share in cash, and (ii) the product of (x) options to purchase 985,881 shares of Talk America common stock that have an exercise price of less than $8.10 per share and (y) $3.91, which is the difference between the merger consideration of $8.10 per share and the options' weighted average exercise price per share of $4.19.

(4) Proposed maximum aggregate value of transaction:

$250,974,763

(5) Total fee paid:

$26,854.30

Fee paid previously with preliminary materials.

Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

**PRELIMINARY PROXY MATERIALS - SUBJECT TO COMPLETION**
**DATE OCTOBER [ ], 2006**

**TALK AMERICA HOLDINGS, INC.**
**6805 ROUTE 202**
**NEW HOPE, PA 18938**
**(215) 862-1500**

Dear Stockholder:

The board of directors (the "Board") of Talk America Holdings, Inc. ("Talk America" or the "Company") has approved a merger agreement providing for the acquisition of the Company by Cavalier Acquisition Corp., an indirectly wholly owned subsidiary of Cavalier Telephone Corporation. If the merger is completed, you will receive $8.10 in cash, without interest, for each share of the Company's common stock you own.

You will be asked, at a special meeting of the Company's stockholders (the "Special Meeting"), to adopt the merger agreement. The Board has approved and declared the merger and the merger agreement advisable, and has declared that it is fair to and in the best interests of Talk America's stockholders that the Company enter into the merger agreement and consummate the merger on the terms and conditions set forth in the merger agreement. The board of directors recommends that Talk America's stockholders vote "FOR" the adoption of the merger agreement.

The time, date and place of the Special Meeting to consider and vote upon a proposal to adopt the merger agreement are as follows:

[ ] local time, [ ], 2006

[ ]

The proxy statement attached to this letter provides you with information about the proposed merger and the Special Meeting of the Company's stockholders. We encourage you to read the entire proxy statement carefully. You may also obtain more information about the Company from documents we have filed with the Securities and Exchange Commission.

YOU ARE REQUESTED TO VOTE YOUR SHARES BY PROMPTLY COMPLETING, SIGNING AND DATING THE ENCLOSED PROXY CARD AND RETURNING IT IN THE ENVELOPE PROVIDED, WHETHER OR NOT YOU PLAN TO ATTEND THE SPECIAL MEETING.

Voting by proxy will not prevent you from voting your shares in person if you subsequently choose to attend the Special Meeting.

Thank you for your cooperation and continued support.

Sincerely,

Gabriel Battista

*Chairman of the Board*

**THIS PROXY STATEMENT IS DATED [ ], 2006**

**AND IS FIRST BEING MAILED TO STOCKHOLDERS ON OR ABOUT [ ], 2006.**

**TALK AMERICA HOLDINGS, INC.**
**6805 ROUTE 202**
**NEW HOPE, PA 18938**
**(215) 862-1500**

**NOTICE OF SPECIAL MEETING OF STOCKHOLDERS**
**To Be Held [ ], 2006**

To the stockholders of
Talk America Holdings, Inc.:

NOTICE IS HEREBY GIVEN that a special meeting of stockholders (the “Special Meeting”) of Talk America Holdings, Inc., a Delaware corporation (“Talk America” or the “Company”), will be held on **[ ]**, 2006, at **[ ]** p.m. Eastern Time, at [ ] for the following purposes:

1. To consider and vote on a proposal to adopt the Agreement and Plan of Merger, dated as of September 22, 2006, by and among the Company, Cavalier Telephone Corporation (the “Parent”) and Cavalier Acquisition Corp., an indirectly wholly owned subsidiary of the Parent (the “Merger Sub”), pursuant to which, upon the merger becoming effective, each share of common stock, par value $0.01 per share, of Talk America (other than shares held in the treasury of the Company or owned by the Parent, the Merger Sub or any wholly owned subsidiary of the Parent or the Company and other than shares held by a stockholder who properly demands statutory appraisal rights) will be converted into the right to receive $8.10 in cash, without interest; and

2. To transact such other business as may properly come before the Special Meeting or any adjournment or postponement thereof.

Only stockholders of record on [ ], 2006 are entitled to notice of and to vote at the Special Meeting and at any adjournment or postponement of the Special Meeting. All stockholders of record are cordially invited to attend the Special Meeting in person.

This notice and proxy statement also constitutes the Company’s notice to its stockholders of the availability of appraisal rights under Section 262 of the Delaware General Corporation Law in connection with the merger.

The adoption of the merger agreement requires the approval of the holders of a majority of the outstanding shares of the Company’s common stock entitled to vote thereon. Even if you plan to attend the Special Meeting in person, we request that you complete, sign, date and return the enclosed proxy and thus ensure that your shares will be represented at the Special Meeting if you are unable to attend. If you are a stockholder of record and do attend the Special Meeting and wish to vote in person, you may withdraw your proxy and vote in person.

By Order of the Board of Directors,

Aloysius T. Lawn, IV
Secretary
New Hope, Pennsylvania
October **[ ]**, 2006

## SUMMARY

The following summary highlights selected information from this proxy statement and may not contain all of the information that may be important to you. Accordingly, we encourage you to read carefully this entire proxy statement, its annexes and the documents referred to or incorporated by reference in this proxy statement. Each item in this summary includes a page reference directing you to a more complete description of that item.

**The Parties to the Merger (Page 10)**

Talk America Holdings, Inc.
6805 Route 202
New Hope, Pennsylvania 18938
215.862.1500

Talk America Holdings, Inc., which we refer to as the Company and Talk America, through its subsidiaries, is a leading competitive communications services provider offering integrated voice and data services, including local, long distance, enhanced voice features and dedicated Internet access services, to commercial (primarily small and medium-sized business) and residential customers. We are focused on markets where we have our own networking assets. Today, we are collocated in 316 end offices in Michigan, Ohio, Kentucky, Tennessee, North Carolina, Louisiana, Mississippi, Alabama, Florida and Georgia.

Our business strategy is to continue to expand our network and grow our “on-net” (that is, our services over our own networking facilities) customer and revenue base through (i) organic growth in our core markets, serving both commercial and residential customers; (ii) additional acquisitions that either supplement our existing markets or offer expansion into new markets; and (iii) enhancement of our product portfolio. Growth in our business, both commercial and residential, on our network will permit us to leverage our investment in our network facilities due to the complementary telecommunication traffic or usage patterns of these customer bases.

Cavalier Telephone Corporation

2134 West Laburnum Avenue
Richmond, Virginia 23227
804.422.4100

Cavalier Telephone Corporation, which we refer to as the Parent and Cavalier, is a privately held Delaware corporation and, through its subsidiaries, is a facilities-based competitive local exchange carrier and provider of access and of integrated communications services in an area focused on the Virginia, Pennsylvania, Delaware, Maryland, New Jersey, New York and District of Columbia markets, and extending to other eastern and midwestern states. Through its subsidiaries and over their own network facilities, Cavalier Telephone Corporation provides business and residential customers a range of services, including local and long distance voice, dedicated data, Internet, access, and internet protocol television services.

Cavalier Acquisition Corp.

c/o Cavalier Telephone Corporation
2134 West Laburnum Avenue
Richmond, Virginia 23227
804.422.4100

Cavalier Acquisition Corp., which we refer to as the Merger Sub, is a Delaware corporation and an indirect wholly owned subsidiary of the Parent that was formed in connection with the merger by the Parent.

**The Special Meeting**

*Time, Place and Date (Page11)*

The Special Meeting will be held on [ ], starting at [ ] local time, at [ ].

*Purpose (Page 11)*

At the Special Meeting, you will be asked to consider and vote upon a proposal to adopt the merger agreement. The merger agreement provides that the Merger Sub will be merged with and into the Company, and that each outstanding share of the Company's common stock (other than shares held in the treasury of the Company or owned by the Merger Sub, the Parent or any wholly owned subsidiary of the Parent or the Company and other than shares held by a stockholder who properly demands statutory appraisal rights) will be converted into the right to receive $8.10 in cash, without interest.

The persons named in the accompanying proxy will also have discretionary authority to vote upon other business, if any, that properly comes before the Special Meeting and any adjournments or postponements of the Special Meeting, including any adjournments or postponements for the purpose of soliciting additional proxies to adopt the merger agreement.

*Record Date and Voting (Page 11)*

You are entitled to vote at the Special Meeting if you owned shares of Talk America common stock at the close of business on [ ], 2006, the record date for the Special Meeting. Each outstanding share of our common stock on the record date entitles the holder to one vote on each matter submitted to stockholders for approval at the Special Meeting. As of the record date, there were [ ] shares of common stock of Talk America entitled to be voted.

*Vote Required (Page 11)*

For us to complete the merger, stockholders holding at least a majority of the shares of our common stock outstanding at the close of business on the record date must vote "FOR" the adoption of the merger agreement.

*Share Ownership of Directors and Executive Officers (Page 42)*

As September 29, 2006, the directors and executive officers of Talk America beneficially owned in the aggregate (excluding stock options) approximately 0.5 % of the combined voting power of the outstanding shares of Talk America common stock entitled to vote at the Special Meeting.

*Voting and Proxies (Page 12)*

Any Talk America stockholder of record entitled to vote may vote by returning the enclosed proxy or by appearing at the Special Meeting. If your shares are held in "street name" by your broker, you should instruct your broker how to vote your shares using the instructions provided by your broker.

*Revocability of Proxy (Page 12)*

Any Talk America stockholder of record who executes and returns a proxy may revoke the proxy at any time before it is voted in any one of the following three ways:

· filing with the Secretary of Talk America, at or before the Special Meeting, a written notice of revocation that is dated a later date than the proxy;

· sending a later-dated proxy relating to the same shares to the Secretary of Talk America, at or before the Special Meeting; or

· attending the Special Meeting and voting in person by ballot.

Simply attending the Special Meeting will not constitute revocation of a proxy. If you have instructed your broker to vote your shares, the above-described options for revoking your proxy do not apply and instead you must follow the directions provided by your broker to change these instructions.

**When the Merger Will Be Completed**

We are working to complete the merger as soon as possible. We anticipate completing the merger by December 31, 2006, subject to receipt of stockholder approval and satisfaction of the other closing conditions under the merger agreement, including the expiration or termination of the waiting period under federal antitrust laws and the receipt of applicable consents from the Federal Communications Commission (the “FCC”) and approvals from certain state public service or public utility commissions (or similar state regulatory agencies) (“State PUCs”).

**Board Recommendation (Page 16)**

After careful consideration, our board of directors:

- has determined that the merger and the merger agreement are advisable, fair to and in the best interests of the Company's stockholders;
- has approved the merger agreement; and
- recommends that Talk America's stockholders vote "FOR" the adoption of the merger agreement.

**Opinion of The Blackstone Group L.P. (Page 16 and Annex B)**

The Blackstone Group L.P. ("Blackstone") has delivered to the Company's board of directors its opinion dated September 22, 2006 to the effect that, as of that date and based upon and subject to the matters and assumptions stated in that opinion, the merger consideration of $8.10 per share in cash to be received by the Company's stockholders pursuant to the merger agreement was fair from a financial point of view to the Company's stockholders. The opinion is not a recommendation as to how any of our stockholders should vote with respect to the merger agreement or the merger. The full text of the written opinion of Blackstone, which sets forth the matters considered and assumptions made in connection with its opinion, is attached as Annex B to this proxy statement. We recommend that you read the entire opinion carefully.

**Financing (Page 23)**

In connection with the merger, the Parent will cause approximately $[ ] million in cash to be paid to our stockholders and holders of stock options and warrants. These payments are expected to be funded by a combination of credit facilities provided to the Parent and its subsidiary, CavTel Holdings, LLC, or CavTel. The Parent and CavTel have received a commitment letter from Wachovia Bank, National Association and Wachovia Capital Markets, LLC pursuant to which Wachovia Bank, National Association has committed to provide the Parent and CavTel with credit facilities in the aggregate amount of $435 million, subject to the satisfaction of the conditions contained in the commitment letter. The closing of the merger and the obligations of the Parent and the Merger Sub under the merger agreement are not, however, conditioned on the Parent's arranging this credit facility or any other financing.

**Treatment of the Company's Common Stock, Options and Warrants (Page 28)**

At the effective time of the merger, each share of the Company's common stock outstanding immediately prior to the effective time of the merger will be canceled and converted into the right to receive $8.10 in cash, without interest.

The merger agreement provides that all outstanding Talk America stock options issued pursuant to Talk America's stock option plans, whether vested or unvested, will be canceled as of the effective time of the merger, and the holder of each stock option that has an exercise price of less than $8.10 will receive from the surviving corporation as soon as practicable thereafter an amount in cash, less any applicable withholding taxes, equal to the product of:

- the number of shares of our common stock subject to each stock option as of the effective time of the merger, multiplied by
- the excess of $8.10 over the exercise price per share of common stock subject to such option.

The merger agreement provides that all outstanding Talk America warrants will be canceled as of the effective time of the merger. While the merger agreement provides for a cash payment for "in-the-money" warrants, similar to the provision for options, there are no warrants outstanding that have an exercise price of less than $8.10.

3

The merger agreement further provides that all payments to holders of the Company's common stock, or of options or warrants for our common stock, will be less any applicable withholding taxes.

**Interests of the Company's Directors and Executive Officers in the Merger (Page 23)**

Some of our executive officers and members of our board of directors have financial interests in the merger that are different from, or in addition to, their interests as our stockholders generally. Our board of directors was aware of these interests and considered the following, among other matters, in approving the merger agreement:

- certain of our executive officers are parties to employment agreements with the Company that provide for severance payments by the Company if they are terminated or they resign for specified reasons prior to or following the effective time of the merger; the terms of the merger agreement permit the payment of up to $4.291 million in such severance payments on the closing date of the merger and the Company proposes to make the full amount of such payments on the closing date;

- under the terms of the merger agreement, our board of directors is permitted, in its sole discretion, to award and pay bonuses to our employees, including our executive officers, at or prior to the closing date of the merger, in an aggregate amount up to $2.5 million; while our board has generally indicated that it expects to award some discretionary bonuses, it has not yet made any decision as to which, if any, persons would be awarded bonuses or any amounts thereof;

- our directors and executive officers will have their vested and unvested stock options canceled as of the effective time of the merger, and they will receive cash payments for each share underlying their options equal to the excess, if any, of $8.10 per share over the exercise price per share of their stock options, less any applicable withholding taxes. As of September 29, 2006, our directors and executive officers hold stock options to acquire an aggregate of 2,940,162 shares, 2,300,164 of which options were vested;

- the merger agreement provides for indemnification and insurance arrangements for our current and former directors and officers that will continue for six years following the effective time of the merger; and

- although Cavalier has not finalized any agreements with any executive officers of Talk America, Cavalier expects to enter into employment agreements with several of our executive officers, whereby each would continue to serve as an officer of the Parent after the closing.

**Rights Agreement (Page 26)**

Prior to the execution of the merger agreement, we amended our rights agreement to exempt the execution of the merger agreement and the consummation of the transactions contemplated by the merger agreement in accordance with the terms thereof.

**Material U.S. Federal Income Tax Consequences (Page 26)**

The merger will be a taxable transaction to you. For U.S. federal income tax purposes, your receipt of cash in exchange for your shares of Talk America common stock generally will cause you to recognize a gain or loss measured by the difference, if any, between the cash you receive in the merger and your adjusted tax basis in your shares of Talk America common stock. You should consult your own tax advisor for a full understanding of how the merger will affect your taxes.

**Regulatory Approvals (Page 27)**

The Hart-Scott-Rodino Act provides that transactions such as the merger may not be completed until certain information has been submitted to the Federal Trade Commission and the Antitrust Division of the U.S. Department of Justice and certain waiting period requirements have been satisfied. On [ ], 2006, the Company and the Parent each filed a Notification and Report Form with the Antitrust Division and the Federal Trade Commission and requested an early termination of the waiting period. If the early termination is not granted and a request for additional information by the relevant antitrust authorities is not made, the waiting period will expire at 11:59 p.m. on [ ], 2006.

Certain of the Company's subsidiaries provide communications services that are regulated by the FCC and/or State PUCs. As providers of such services, those subsidiaries hold authorizations issued by the FCC and State PUCs. Permission from or notices to many of these regulatory agencies is required to transfer control of the subsidiaries and therefore to complete the transfer of control of the Company.

Under the Communications Act of 1934, as amended, the FCC must approve the transfer of control to the Parent of the Company and those subsidiaries of the Company that hold FCC licenses and authorizations. The FCC must determine whether the Parent is qualified to control such licenses and authorizations and whether the transfer is consistent with the public interest. The Company and the Parent filed a transfer of control application with the FCC on **[ ]**, 2006.

Certain subsidiaries of the Company also hold certificates and authorizations issued by State PUCs in all U.S. states (except Alaska) and the District of Columbia, where they provide intrastate telecommunications services. Many of the State PUCs in each of the states where Company subsidiaries operate must either approve the transactions contemplated by the merger agreement or require that formal notice of the transactions be provided to them. As of **[ ]**, 2006, the Company and the Parent had filed the necessary applications and notices with these State PUCs.

**Procedure for Receiving Merger Consideration (Page 29)**

As soon as practicable after the effective time of the merger, a paying agent appointed by the Parent will mail a letter of transmittal and instructions to Talk America stockholders. The letter of transmittal and instructions will tell you how to surrender your Talk America common stock certificates in exchange for the merger consideration. You should not return your stock certificates with the enclosed proxy card, and you should not forward your stock certificates to the paying agent without a letter of transmittal.

**No Solicitation of Transactions (Page 34)**

The merger agreement contains restrictions on our ability to solicit or engage in discussions or negotiations with a third party regarding specified transactions involving the Company. Notwithstanding these restrictions, under certain circumstances, our board of directors may respond to an unsolicited written bona fide proposal for an alternative acquisition or terminate the merger agreement and enter into an acquisition agreement with respect to a superior proposal.

**Conditions to Closing (Page 37)**

Before we can complete the merger, a number of conditions must be satisfied. These include, among others:

- the receipt of Company stockholder approval;
- the absence of, or of any pending proceeding seeking, any governmental order, decree, judgment, injunction or other ruling that prevents or prohibits the consummation of the merger;
- the expiration or termination of the waiting period under the Hart-Scott-Rodino Act;
- the receipt of applicable consents from the FCC;
- the receipt of applicable approvals from the State PUCs that regulate the Company's business or the business of any of its subsidiaries;
- the truth and correctness of our representations and warranties as of the date of the merger agreement and, except where the failure of our representations and warranties to be true and correct would not reasonably be expected to

have a material adverse effect on us and our subsidiaries, individually or in the aggregate, the truth and correctness of our representations and warranties (without giving effect for any materiality or material difference qualification therein) as of the closing date or as of the earlier date for such representations and warranties as expressly relate to an earlier date, and the truth and correctness of our representations and warranties with respect to authority and approvals, absence of material adverse change and brokers as of the closing date as if made on and as of the closing date;

- since September 22, 2006, the date of execution of the merger agreement, no “material adverse effect” with respect to the Company shall have occurred and be continuing.
- we meet a defined minimum financial performance measure based on our operating income for the quarter ended September 30, 2006 as adjusted for a number of items; and
- the performance and compliance, in all material respects, by us of our agreements and conditions in the merger agreement.

**Termination of the Merger Agreement (Page 38)**

Talk America and the Parent may agree in writing to terminate the merger agreement at any time without completing the merger, even after the stockholders of Talk America have adopted the merger agreement. The merger agreement may also be terminated in certain other circumstances, including:

- by either the Parent or the Company if:
- our stockholders fail to adopt the merger agreement at the Special Meeting of the stockholders or any adjournment of the Special Meeting;
- the closing has not occurred on or before January 31, 2007, which we refer to as the “termination date,” so long as the failure to complete the merger is not the result of the failure of the terminating party to comply with the terms of the merger agreement;
- there is any law or final, non-appealable government order, decree or ruling that prevents completion of the merger, so long as such law, government order, decree or ruling is not the result of the failure of the terminating party to fulfill its obligations under the merger agreement; or
- there is a breach by the non-terminating party of its representations, warranties, covenants or agreements in the merger agreement such that the closing conditions would not be satisfied, which breach has not been cured within 20 business days (or is incapable of being cured before the termination date);
- by the Company, prior to adoption of the merger agreement, if we receive a superior proposal in accordance with the terms of the merger agreement, but only after we have provided the Parent a three-business-day period to make an offer that is at least as favorable as the superior proposal;
- by the Parent, if:
- our board of directors withdraws or modifies its recommendation that the Company’s stockholders vote to adopt the merger agreement or recommends or approves another takeover proposal;
- our board of directors fails to include in our proxy statement its recommendation that the Company’s stockholders vote to adopt the merger agreement;
- our board of directors fails to publicly reaffirm its recommendation of the merger agreement and the merger within ten days after the Parent has requested in writing that our board of directors reaffirm its recommendation;

- the Company fails to recommend rejection of a tender or exchange offer within ten days after the commencement of such tender or exchange offer;

- a takeover proposal is publicly announced and the Company fails to issue a press release within ten days after the announcement that reaffirms the recommendation of our board of directors that the Company's stockholders vote in favor of the merger; or

- the Company fails to call, give notice of, convene and hold the special stockholders' meeting and timely mail this proxy statement, which is not cured within 10 business days following receipt by the Company of a notice of such breach.

**Termination Fees and Expenses (Page 39)**

Under certain circumstances, in connection with the termination of the merger agreement, we will be required to pay the Parent a termination fee of $6.25 million or up to an additional $1.25 million for reimbursement of expenses or both.

**Market Price of the Company's Common Stock (Page 41)**

Our common stock is quoted on the Nasdaq National Market ("Nasdaq") under the trading symbol "TALK". On September 21, 2006, which was the last trading day before we announced the merger, the Company's common stock closed at $6.57 per share. On [ ], 2006, which was the last trading day before the date of this proxy statement, the Company's common stock closed at $[ ] per share.

**Dissenters' Rights of Appraisal (Page 44 and Annex C)**

Delaware law provides you with appraisal rights in connection with the merger. This means that you are entitled to have the value of your shares determined by the Delaware Court of Chancery and to receive payment based on that valuation. The ultimate amount you receive as a dissenting stockholder in an appraisal proceeding may be more or less than, or the same as, the amount you would have received under the merger agreement.

To exercise your appraisal rights, you must deliver a written objection to the merger to the Company at or before the vote on the adoption of the merger agreement at the Special Meeting and you must not vote in favor of the adoption of the merger agreement. Your failure to follow exactly the procedures specified under Delaware law will result in the loss of your appraisal rights.

A copy of Section 262 of the General Corporation Law of the State of Delaware (the "DGCL") is attached to this proxy statement as Annex C.

## QUESTIONS AND ANSWERS ABOUT THE SPECIAL MEETING AND THE MERGER

The following discussion addresses briefly some questions you may have regarding the Special Meeting and the proposed merger. These questions and answers may not address all questions that may be important to you as a stockholder of Talk America Holdings, Inc. Please refer to the more detailed information contained elsewhere in this proxy statement, the annexes to this proxy statement and the documents referred to or incorporated by reference in this proxy statement. In this proxy statement, the terms "Talk America," "Company", "we," "our," "ours" and "us" refer to Talk America Holdings, Inc. and its subsidiaries.

**Q:** **What is the proposed transaction?**

A:

The proposed transaction is the acquisition of the Company pursuant to an Agreement and Plan of Merger (the “merger agreement”), dated as of September 22, 2006, by and among the Company, Cavalier Telephone Corporation, a Delaware corporation (the “Parent”), and Cavalier Acquisition Corp., a Delaware Corporation, an indirect wholly-owned subsidiary of the Parent (the “Merger Sub”). Once the merger agreement has been adopted by Talk America’s stockholders and the other closing conditions under the merger agreement have been satisfied or waived, the Merger Sub will merge with and into Talk America (the “merger”). Talk America will be the surviving corporation in the merger (the “surviving corporation”) and will become a wholly owned subsidiary of the Parent.

**Q: What will I receive in the merger?**

A: Upon completion of the merger, you will receive $8.10 in cash, without interest, for each share of our common stock that you own. For example, if you own 100 shares of our common stock, you will receive $810 in cash in exchange for your Talk America shares.

**Q: Where and when is the Special Meeting?**

A: The Special Meeting will take place at [ ], on [ ], at [ ] local time.

**Q: What vote of our stockholders is required to adopt the merger agreement?**

A: For us to complete the merger, stockholders holding at least a majority of the shares of our common stock outstanding at the close of business on the record date must vote "FOR" the adoption of the merger agreement.

**Q: How does the Company's board of directors recommend that I vote?**

A: Our board of directors recommends that you vote "FOR" the proposal to adopt the merger agreement. You should read "The Merger — Reasons for the Merger" for a discussion of the factors that our board of directors considered in deciding to recommend the adoption of the merger agreement.

**Q: What do I need to do now?**

A: We urge you to read this proxy statement carefully, including its annexes, and to consider how the merger affects you. If you are a stockholder of record, then you should mail your completed, dated and signed proxy card in the enclosed return envelope as soon as possible so that your shares can be voted at the Special Meeting of our stockholders. If you fail to return your proxy card and you do not vote in person at the Special Meeting, it will have the same effect as voting against the merger. You are urged to act promptly in returning your proxy.

**Q: If my shares are held in "street name" by my broker, will my broker vote my shares for me?**

A: Yes, but only if you provide instructions to your broker on how to vote. You should follow the directions provided by your broker regarding how to instruct your broker to vote your shares. Without those instructions, your shares will not be voted, which will have the same effect as voting against the merger.

**Q: Can I change my vote after I have mailed my proxy card?**

A: Yes. You can change your vote at any time before your proxy is voted at the Special Meeting. You may revoke your proxy by notifying the Secretary of Talk America in writing or by submitting a new proxy card, in each case dated after the date of the proxy being revoked. In addition, your proxy may be revoked by attending the Special Meeting and voting in person. However, simply attending the Special Meeting will not revoke your proxy. If you have instructed a broker to vote your shares, the above-described options for changing your vote do not apply and instead you must follow the instructions received from your broker to change your vote.

**Q: Are appraisal rights available?**

A: Yes. Under Delaware law, holders of our common stock who do not vote in favor of adopting the merger agreement will have the right to seek appraisal of the fair value of their shares as determined by the Delaware Court of Chancery if the merger is completed, but only if they submit a written demand for an appraisal prior to the vote on the adoption of the merger agreement and they comply with the Delaware law procedures explained in this proxy statement. This appraisal amount could be more than, the same as or less than the amount a stockholder would be entitled to receive under the terms of the merger agreement.

**Q: Is the merger expected to be taxable to me?**

A: Yes. The receipt of $8.10 in cash for each share of our common stock pursuant to the merger will be a taxable transaction for U.S. federal income tax purposes. For U.S. federal income tax purposes, generally you will recognize a gain or loss as a result of the merger measured by the difference, if any, between $8.10 per share and your adjusted tax basis in that share. You should read "The Merger — Material U.S. Federal Income Tax Consequences" for a more complete discussion of the U.S. federal income tax consequences of the merger. Tax matters can be complicated, and the tax consequences of the merger to you will depend on your particular tax situation. You should also consult your tax advisor on the tax consequences of the merger to you.

**Q: What will the holders of the Company's stock options and warrants receive in the merger?**

A: As of the effective time of the merger, all stock options and warrants to purchase shares of Company common stock will be canceled and the holder of each stock option or warrant, as the case may be, with a per share exercise price lower than the $8.10 per share merger consideration will be entitled to receive a cash payment in an amount equal to the excess, if any, of the $8.10 per share merger consideration over the exercise price of such option or warrant, less any applicable withholding taxes. However, none of the warrants outstanding has a per share exercise price lower than the merger consideration, so no payments will be made in respect of any warrants.

**Q: When do you expect the merger to be completed?**

A: We are working toward completing the merger as quickly as possible, and we anticipate that it will be completed by December 31, 2006. In order to complete the merger, we must obtain stockholder approval, and the other closing conditions under the merger agreement must be satisfied, including the expiration or termination of the waiting period under federal antitrust laws and the receipt of applicable approvals from the FCC and the State PUCs that regulate the Company's business or the business of any of its subsidiaries. See "The Merger Agreement — Conditions to the Merger."

**Q: Should I send in my stock certificates now?**

A: No. Shortly after the merger is completed, you will receive a letter of transmittal with instructions informing you how to send your stock certificates to the paying agent in order to receive the merger consideration. You should use the letter of transmittal to exchange Talk America stock certificates for the merger consideration to which you are entitled as a result of the merger. DO NOT SEND ANY STOCK CERTIFICATES WITH YOUR PROXY.

**Q: Who can help answer my other questions?**

A: If you have more questions about the merger, you should contact Aloysius T. Lawn, IV, Executive Vice President -- General Counsel and Secretary, at (215) 862-1500. If your broker holds your shares, you should also call your broker for additional information.

## CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING INFORMATION

This proxy statement and the documents to which we refer you in this proxy statement contain forward-looking statements based on estimates and assumptions. Forward-looking statements include information concerning possible or assumed future results of operations of the Company, the expected completion and timing of the merger and other information relating to the merger. There are forward-looking statements throughout this proxy statement, including, among others, under the headings "Summary," "The Merger" and "The Merger — Opinion of The Blackstone Group L.P.," and in statements containing the words "believes," "plans," "expects," "anticipates," "intends," "estimates" or other similar expressions. For each of these statements, the Company claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. You should be aware that forward-looking statements involve known and unknown risks and uncertainties. Although we believe that the expectations reflected in these forward-looking statements are reasonable, we cannot assure you that the actual results or developments we anticipate will be realized or, even if realized, that they will have the expected effects on the business or operations of the Company. These forward-looking statements speak only as of the date on which the statements were made, and we undertake no obligation to publicly update or revise any forward-looking statements made in this proxy statement or elsewhere as a result of new information, future events or otherwise. In addition to other factors and matters contained or incorporated in this document, we believe the following factors could cause actual results to differ materially from those discussed in the forward-looking statements:

- the risk that the merger may not be consummated in a timely manner if at all;
- the occurrence of any event, change or other circumstance that could give rise to the termination of the merger agreement;

- the outcome of any legal proceeding against us and others that may be instituted following announcement of the merger agreement;
- risks related to diverting management's attention from ongoing business operations;
- our dependence on key personnel;

· risks regarding employee retention;

· changes in regulatory requirements;

· the absence of certainty regarding the receipt of required regulatory approvals or the timing or terms of such regulatory approvals; and

· other risks detailed in our current filings with the Securities and Exchange Commission (the "SEC"), including our most recent filings on Form 10-K or Form 10-Q, which discuss these and other important risk factors concerning our operations.

## THE PARTIES TO THE MERGER

### Talk America Holdings, Inc.

Talk America Holdings, Inc., which we refer to as the Company and Talk America, through its subsidiaries, is a leading competitive communications services provider offering integrated voice and data services, including local, long distance, enhanced voice features and dedicated Internet access services, to commercial (primarily small and medium-sized business) and residential customers. We are focused on markets where we have our own networking assets. Today, we are collocated in 316 end offices in Michigan, Ohio, Kentucky, Tennessee, North Carolina, Louisiana, Mississippi, Alabama, Florida and Georgia.

The address of our executive office is 6805 Route 202, New Hope, Pennsylvania 18938 and our telephone number is 215.862.1500.

Our business strategy is to continue to expand our network and grow our "on-net" (that is, our services over our own networking facilities) customer and revenue base through (i) organic growth in our core markets, serving both commercial and residential customers; (ii) additional acquisitions that either supplement our existing markets or offer expansion into new markets; and (iii) enhancement of our product portfolio. Growth in our business, both commercial and residential, on our network will permit us to leverage our investment in our network facilities due to the complementary telecommunication traffic or usage patterns of these customer bases.

### Cavalier Telephone Corporation

Cavalier Telephone Corporation, which we refer to as the Parent and Cavalier, is a privately held Delaware corporation with its principal executive offices at 2134 West Laburnum Avenue, Richmond, Virginia 23227. Its telephone number is 804.422.4100. Parent, through its subsidiaries, is a facilities-based competitive local exchange carrier and provider of access and of integrated communications services in an area focused on the Virginia, Pennsylvania, Delaware, Maryland, New Jersey, New York and District of Columbia markets, and extending to other eastern and midwestern states. Through its subsidiaries and over their own network facilities, Cavalier Telephone Corporation provides business and residential customers a range of services, including local and long distance voice, dedicated data, Internet, access, and internet protocol services.

### Cavalier Acquisition Corp.

Cavalier Acquisition Corp., which we refer to as Merger Sub, is a Delaware corporation and an indirect wholly owned subsidiary of the Parent that was formed in connection with the merger by the Parent. Merger Sub's address is c/o Cavalier Telephone Corporation, 2134 West Laburnum Avenue, Richmond, Virginia 23227. Its telephone number is 804.422.4100.

## THE SPECIAL MEETING

### Time, Place and Purpose of the Special Meeting

This proxy statement is being furnished to our stockholders as part of the solicitation of proxies by our board of directors for use at the Special Meeting to be held on [ ], 2006, starting at [ ] local time, at [ ]. The purpose of the Special Meeting is for our stockholders to consider and vote upon a proposal to adopt the merger agreement. A copy of the merger agreement is attached to this proxy statement as Annex A. This proxy statement, the notice of the Special Meeting and the enclosed form of proxy are first being mailed to our stockholders on [ ], 2006.

### Record Date, Quorum and Voting Power

The holders of record of Talk America common stock at the close of business on [ ], 2006, the record date for the Special Meeting, are entitled to receive notice of, and to vote at, the Special Meeting. As of the record date, there were [ ] shares of our common stock issued and outstanding, all of which are entitled to be voted at the Special Meeting.

Each outstanding share of our common stock on the record date entitles the holder to one vote on each matter submitted to stockholders for approval at the Special Meeting.

The holders of a majority of the outstanding shares of our common stock on the record date, represented in person or by proxy, will constitute a quorum for purposes of the Special Meeting. A quorum is necessary to hold the Special Meeting. Once a share is represented at the Special Meeting, it will be counted for the purpose of determining a quorum at the Special Meeting and any adjournment or postponement of the Special Meeting. However, if a new record date is set for the adjourned Special Meeting, then a new quorum will have to be established.

### Required Vote

Completion of the merger requires the adoption of the merger agreement by the affirmative vote of the holders of a majority of the shares of our common stock outstanding on the record date.

In order for your shares of our common stock to be included in the vote, if you are a stockholder of record, you must vote your shares by completing, signing, dating and returning the enclosed proxy or by voting in person at the Special Meeting.

If your shares are held in “street name” by your broker, you should instruct your broker how to vote your shares using the instructions provided by your broker. If you have not received such voting instructions or require further information regarding such voting instructions, contact your broker and they can give you directions on how to vote your shares. Under the rules of Nasdaq, brokers who hold shares in “street name” for customers may not exercise their voting discretion with respect to the approval of matters such as the merger proposal, and, therefore, absent specific instructions from the beneficial owner of such shares, brokers are not empowered to vote such shares with respect to the approval of such proposals (i.e., “broker non-votes”). Shares of Company common stock held by persons attending the Special Meeting but not voting, or shares for which the Company has received proxies with respect to which holders have abstained from voting, will be considered abstentions. Abstentions and properly executed broker non-votes will be treated as shares that are present and entitled to vote at the Special Meeting for purposes of determining whether a quorum exists but will have the same effect as votes “AGAINST” the adoption of the merger agreement.

As of September 29, 2006, our directors and executive officers beneficially owned (excluding stock options), in the aggregate, 166,953 shares of our common stock, representing approximately 0.5% of the combined voting power of the outstanding shares of our common stock. The directors and executive officers have informed Talk America that they intend to vote all of their shares of our common stock “FOR” the adoption of the merger agreement.

11

**Proxies; Revocation**

If you vote your shares of our common stock by signing a proxy, your shares will be voted at the Special Meeting in accordance with the instructions given. If no instructions are indicated on your signed proxy card, your shares of our common stock will be voted “FOR” the adoption of the merger agreement.

You may revoke your proxy at any time before the vote is taken at the Special Meeting. To revoke your proxy, you must advise our Secretary in writing or deliver a new proxy, in each case dated after the date of the proxy you wish to revoke, or attend the Special Meeting and vote your shares in person. Mere attendance at the Special Meeting will not by itself constitute revocation of a proxy.

If you have instructed your broker to vote your shares, the above-described options for revoking your proxy do not apply, and instead you must follow the directions provided by your broker to change these instructions.

Talk America does not expect that any matter other than the proposal to adopt the merger agreement will be brought before the Special Meeting. If, however, such a matter is properly presented at the Special Meeting or any adjournment or postponement of the Special Meeting, the persons appointed as proxies will have authority to vote the shares represented by duly executed proxies in accordance with their discretion and judgment.

Talk America will pay the cost of this proxy solicitation. In addition to soliciting proxies by mail, directors, officers and employees of Talk America may solicit proxies personally and by telephone, facsimile or other electronic means of communication. These persons will not receive additional or special compensation for such solicitation services. Talk America will, upon request, reimburse brokers, banks and other nominees for their expenses in sending proxy materials to their customers who are beneficial owners and obtaining their voting instructions.

**Adjournments and Postponements**

Although it is not expected, the Special Meeting may be adjourned or postponed for the purpose of soliciting additional proxies. Any adjournment or postponement may be made without notice by an announcement made at the Special Meeting. Any signed proxies received by Talk America will be voted in favor of an adjournment or postponement in these circumstances. Any adjournment or postponement of the Special Meeting for the purpose of soliciting additional proxies will allow Talk America stockholders who have already sent in their proxies to revoke them at any time prior to their use.

## THE MERGER

**Background of the Merger**

On several occasions in September 2004, management representatives of the Company met with management representatives of Cavalier to exchange information about their respective companies and to discuss a possible business combination of the companies. These discussions did not lead to any proposal and ended in late 2004.

On April 5, 2006, by e-mail to Gabriel Battista, Chairman of our board of directors, Brad Evans, Chief Executive Officer of Cavalier, indicated an interest in discussing the Company with Mr. Battista. Mr. Battista referred him to Edward Meyercord, Chief Executive Officer of the Company, to explore any potential transactions, and, on April 18, 2006, Messrs. Evans and Meyercord had a general telephone discussion about the current status of their respective companies’ businesses. No potential transactions were discussed, nor was financial information concerning the Company exchanged.

In early May 2006, Mr. Meyercord, at the direction of our board of directors, discussed with representatives of The Blackstone Group, L.P. and other potential financial advisors, their potential engagement to provide financial advisory services to the Company and our board. On May 19, 2006, Mr. Evans sent an email to Mr. Meyercord informing him that Cavalier had hired Jefferies & Company to represent them as financial advisor and expressed a desire to discuss potential transaction structures.

On May 31, 2006, Mr. Evans and James F. Wade, a director of Cavalier, had a teleconference with Mr. Meyercord and David Zahka, Chief Financial Officer of the Company, to say that Cavalier would be interested in pursuing further discussions about a possible business combination transaction between the Company and Cavalier.

With the authorization of the Chairman of our board of directors, on June 7, 2006, Mr. Meyercord and Mr. Zahka met with Mr. Evans and David Whitt, Chief Financial Officer of Cavalier, and held general discussions regarding their respective businesses and organizations. No financial information concerning the companies was exchanged at the meeting or immediately thereafter. On June 12, 2006, Mr. Evans contacted Mr. Meyercord to discuss certain follow-up questions with regard to the Company's business and management team. On June 14, 2006, Mr. Meyercord met with Messrs Evans and Wade to discuss a potential acquisition of the Company and Mr. Meyercord's role therein.

On June 19, 2006, Mr. Evans sent an email to Mr. Meyercord indicating that a proposal would be sent to our board of directors offering to purchase the common stock of the Company at $10 per share based on a projected 2006 EBITDA for the Company of $65 million and assuming synergies of $15 million per year.

In the meantime, on June 16, 2006, the Company entered into a letter agreement with Blackstone, engaging them to provide financial advisory services to the Company and our board in connection with the evaluation of strategic alternatives for the Company, including further acquisitions by the Company, dispositions by the Company and business combinations involving the Company.

From June 21 through June 27, 2006, the Company's management met to consider the Company's recent performance and the impact of changes in the competitive environment in the Company's principal service areas. As a result of these considerations, the Company's management recommended to our board that the principal focus of the Company's businesses be changed from marketing standalone voice services to the marketing of a bundle of broadband and voice services and that the Company's existing public financial guidance for 2006 be revised downward.

On June 23, 2006, Mr. Battista received a letter from Cavalier stating that it was a "non-binding, preliminary indication of interest in connection with the possible acquisition of" the Company, with "a preliminary, non-binding offer price reflecting an enterprise value in the range of $288.8 to $301.1 million," stated to equate "to a price per share of $9.50 to $10.20," which would be payable 100% in cash, and to represent "a premium of 30% to 40% to [the Company's] current stock price." The letter stated that Cavalier's analysis of a possible transaction had relied solely upon publicly available information on the Company and that further discussions and due diligence were required to complete Cavalier's evaluation of the Company. The closing sale price of the Company's common stock on Nasdaq on June 23, 2006 was $7.27.

On June 28, 2006, our board of directors met to consider management's report on the Company's recent performance, management's recommendation to change the principal focus of the Company's businesses from marketing standalone voice services to the marketing of a bundle of broadband and voice services, and the reduction of the Company's financial guidance for 2006. At the meeting, Mr. Battista also reviewed with our board the recent communications that had been had with Cavalier representatives, including the June 23 indication of interest letter received from Cavalier. Our board generally discussed the potential prospects of such a transaction, as well as the prospects of possible acquisitions by the Company in the Southeast, and authorized continued discussions with Cavalier and giving Cavalier the opportunity to conduct limited due diligence to permit them to better assess their valuation of the Company, particularly in light of the revised financial guidance that the Company would announce that day. Our board also directed that, because Mr. Meyercord might be an interested party in any transaction with Cavalier with respect to the terms of any transaction between the Company and Cavalier, Mr. Battista lead any further communications and negotiations with Cavalier with respect to any transaction between the parties, and that Mr. Meyercord henceforth not participate in any transaction discussions or negotiations, beyond his participation in Company due diligence information disclosures. Mr. Battista communicated to Mr. Evans of Cavalier that he, and not Mr. Meyercord, would be supervising any transaction discussions and negotiations with Cavalier and that our board would consider Cavalier's proposal in due course along with its ongoing consideration of other strategic alternatives.

On June 28, 2006, the Company issued a press release announcing the strategy shift to the marketing of a bundle of broadband and voice services and the downwardly revised financial guidance for the second quarter and full year 2006. The closing sale price of the Company's common stock on Nasdaq on June 28, 2006 was $6.67.

On July 7 and 12, 2006, our board of directors met with its financial advisor, Blackstone, to review and consider various strategic alternatives for the Company, including continuing as a standalone enterprise, growing through acquisitions, with a review of several potential acquisition candidates, and the sale of the Company, including a sale in the price range indicated in the June 23 Cavalier interest indication. Our board reached no conclusion in the meetings to pursue any one strategy, but did determine that it would be desirable, whichever course it might ultimately determine to pursue, not to discourage a future Cavalier offer and, in that regard, to make limited non-public information available to Cavalier's representatives if Cavalier executed a confidentiality agreement. After the board meeting on July 12, Mr. Battista, on behalf of our board, advised Cavalier of this determination.

On July 14, 2006, the Company received from Cavalier a preliminary due diligence request list.

Cavalier signed a confidentiality agreement with the Company on July 19, 2006, and, from July 19 to 21, the Company compiled non-public information concerning the Company. On July 21, 2006, senior management of the Company traveled to Cavalier's offices in Richmond, VA to present due diligence information to the management of Cavalier. During that meeting, Cavalier conducted due diligence discussions with the Company with respect to the non-public information and general matters relating to the Company's business. On July 27, 2006, Cavalier delivered to Mr. Battista a letter stating that it was a "revised non-binding, preliminary indication of interest in connection with the possible acquisition of" the Company, with "a preliminary, non-binding offer price reflecting an enterprise value of $243 million or $8 per share," which would be payable 100% in cash, and was stated to represent "a 34% premium to current share price." The letter stated that Cavalier's final proposal would "not be subject to any financing contingency," that the indication of interest was "based on Cavalier's initial discussions with members of the Company's management and Board of Directors and the review of non-public information as well as available public information of the Company" and was subject, among other things, to Cavalier's satisfactory completion of its due diligence, and that Cavalier proposed to negotiate necessary documentation in parallel with the completion of its due diligence, which it anticipated would be within 30 days after the letter.

At meetings on August 1 and 8, 2006, our board met with Blackstone to consider Blackstone's review and analysis of strategic alternatives for the Company, including the latest Cavalier indication of interest at $8 per share. On August 8, 2006, our board authorized Mr. Battista to advise Cavalier that it would give Cavalier access to more detailed due diligence information and would consider proceeding further with Cavalier to determine whether there could be an acceptable definitive proposal only if Cavalier would increase the level of its per share offer price above $8.00. The board also authorized Blackstone Group to conduct discussions with a limited group of potential acquirors and authorized Company counsel to review any drafts of transaction documents that Cavalier might propose. Mr. Battista and Mr. Evans spoke several times between August 8 and 11 to discuss our board's position that further discussions and due diligence could only proceed if Cavalier would increase the share offer price above $8.00. Mr. Evans advised that Cavalier was prepared to increase their interest level to $8.50 per share. Mr. Battista consulted with each member of our board (except Mr. Meyercord) about his discussions with Mr. Evans and whether an increase of the per share offer price to $8.50 would be acceptable to such member as a condition to agreeing to provide Cavalier more detailed due diligence information and proceeding further with Cavalier to determine whether an acceptable definitive proposal could be reached. Each director consulted agreed that the $8.50 proposal would be acceptable and Mr. Battista so advised Cavalier. On August 11, 2006, Cavalier delivered to the Company a revised letter, dated August 12, 2006, in the same form as its July 27 letter, except that it included an $8.50 per share price.

On August 15, 2006, the Company received an extensive business and legal due diligence request list from Cavalier. On August 17, 2006, representatives from Cavalier traveled to the Company's headquarters in New Hope, PA to meet with members of the Company's management and to review due diligence items. From August 17 through September

10, 2006, Cavalier conducted its legal and business due diligence, including meetings with management representatives of the Company, and the parties and their counsel began negotiation of the terms of a proposed definitive merger agreement and related documentation, including the representations and warranties to be made by the Company, the covenants regarding the operations of the Company between the execution of the merger agreement and the closing of the merger and the conditions to the closing of the merger.

On September 5, 2006, Mr. Meyercord met with members of Cavalier's board of directors and management in Richmond, VA to discuss the Company's business and overall industry dynamics.

During the morning and early afternoon of September 11, 2006, Messrs. Battista and Evans had several meetings and communications regarding the proposed Cavalier transaction. Mr. Evans reviewed a number of issues that had been noted in the course of Cavalier's due diligence that adversely affected their previous valuation of the Company. After discussion, Mr. Evans advised Mr. Battista that Cavalier's "best and final offer" was $8.10 per share and that time was of the essence in getting to a definitive merger agreement if the Company was interested in pursuing the Cavalier proposal further, setting a September 20 deadline.

Our board of directors met later in the afternoon of September 11, 2006 to discuss the latest proposal and its implications, as well as to review with Blackstone the results of Blackstone's inquiries to a select group of other potential acquirers of the Company and certain other individuals that Blackstone considered knowledgeable about the industry and the potential market for companies such as the Company. Blackstone reported to the board that its limited inquiries and discussions to date with other parties indicated a lack of interest in the acquisition of the Company generally and specifically at any value level comparable to the values being discussed with Cavalier. The board also discussed recent regulatory developments, including a forbearance petition recently filed by Verizon, and authorized Blackstone to widen the scope of their inquiries of other potential acquirers and authorized Company counsel to finalize the form of the proposed definitive merger agreement.

Our board met on September 19 and 20, 2006 to discuss the status of the negotiations and the results of Blackstone's further survey of potential interest in a transaction with the Company, which was reported by Blackstone to indicate no more interest than had been indicated at the last meeting notwithstanding the broadening of the survey, to consider Blackstone's advice as to the fairness of the proposed transaction from a financial point of view and to review the terms of the proposed merger agreement and other matters. Following the meetings, Mr. Battista and representatives of Blackstone had several discussions with Cavalier representatives to negotiate some of the terms of the proposed merger agreement. The board met again on the morning of September 22, 2006 to review the final terms of the proposed transaction and the final form of the merger agreement. At that meeting, Blackstone delivered its opinion to our board that the consideration to be paid to the holders of common stock in the merger agreement was fair from a financial point of view to such holders of common stock, and the board, with Mr. Meyercord recusing himself from the deliberations and the vote, approved the merger agreement and the transactions contemplated thereby, including the merger of the Merger Sub into the Company.

In the early afternoon of September 22, 2006, the Company, Merger Sub and Parent executed the merger agreement. The parties then issued press releases announcing the execution of the definitive agreement.

On September 28, 2006, the Company received an unsolicited letter from Sun Capital Securities Group, LLC ("Sun Capital") proposing "to purchase for cash all of the outstanding shares of Company Common Stock for $9.00 per share," subject to the terms and conditions set forth therein, including Sun Capital's satisfactory completion of due diligence.

Also on September 28, 2006 and in response to the receipt of the Sun Capital letter, our board of directors, as permitted by an exception to the general "non-solicitation" terms of the merger agreement, made the necessary determinations in respect of the Sun Capital letter and the proposal contained therein so as to permit the Company to furnish information about the Company to Sun Capital and its representatives pursuant to a confidentiality agreement with Sun Capital and to participate in discussions and negotiations with Sun Capital in respect of its proposal. Following this action, the Company entered into a confidentiality agreement with Sun Capital and began to make available to Sun Capital information regarding the Company.

**Reasons for the Merger**

After careful consideration, the Company's board of directors has approved and determined the merger agreement advisable and has declared that the merger and the merger agreement are fair to and in the best interests of the Company's stockholders. In the course of reaching its decision to approve the merger agreement, the Company's board of directors consulted with senior management and the Company's financial and legal advisors and considered a number of factors, including the following:

· the Company's business, operations, financial condition, strategy and prospects, as well as the risks involved in achieving those prospects, the nature of the competitive local exchange industry and general industry, economic and market conditions, both on a historical and on a prospective basis;

· the potential value that might result from other alternatives available to the Company, including the alternative of remaining a stand-alone, independent company, as well as the risks and uncertainties associated with those alternatives;

· the consideration offered in the merger compared to the Company's stand-alone value, particularly in light of developments and anticipated developments in the Company's business and competitive position and in the competitive local exchange industry generally, and in light of board concerns as to the prospects of successful implementation of the Company's recently revised marketing strategy and the ability of management to achieve their forecasted results;

- the efforts made by the Company and its advisors to negotiate and execute a merger agreement favorable to the Company;

15

- the financial and other terms and conditions of the merger agreement as reviewed by our board of directors with our financial and legal advisors (see “The Merger Agreement”) and the fact that these terms and conditions were the product of arm’s-length negotiations between the parties;

- the current and historical market prices of the Company’s common stock, including the market price of the Company’s common stock relative to those of other industry participants and general market indices, and the fact that the cash merger price of $8.10 per share represents a substantial premium to the average closing share prices of the Company’s common stock over the 30-, 60- and 90-day periods preceding September 21, 2006, the last trading day prior to the execution of the merger agreement;

- the financial presentation of Blackstone, including its opinion to the effect that, as of that date and based upon and subject to the matters and assumptions stated in that opinion, the merger consideration of $8.10 per share in cash to be received by the Company’s stockholders pursuant to the merger agreement was fair, from a financial point of view, to the Company’s stockholders (see “The Merger — Opinion of The Blackstone Group L.P.”);

- the fact that the merger consideration is all cash, so that the transaction allows the Company’s stockholders to immediately realize a fair value, in cash, for their investment;

- the fact that an all-cash transaction would be taxable to the Company’s stockholders for U.S. federal income tax purposes;

- the fact that the Company could terminate the merger agreement, prior to the stockholder vote, in order to approve a transaction proposal by a third party on terms more favorable to the Company’s stockholders than the merger with the Merger Sub, after having given the Parent an opportunity to match the third-party proposal and upon the payment to the Parent of a $6.25 million termination fee and up to an additional $1.25 million for reimbursement of expenses (see “The Merger Agreement — Termination” and “The Merger Agreement — Termination Fees and Expenses”);

- the risks and costs to the Company if the merger does not close, including the diversion of management and employee attention, potential employee attrition and the potential effect on business and customer relationships;

- the interests of the Company’s officers and directors in the merger; and

- the restrictions on the conduct of the Company’s business prior to the completion of the merger, requiring the Company to conduct its business in the ordinary course consistent with past practice, subject to specific limitations, which may delay or prevent the Company from undertaking business opportunities that may arise pending completion of the merger.

The foregoing discussion summarizes the material factors considered by our board of directors in its consideration of the merger, including factors that support the merger as well as those that may weigh against it. In view of the wide variety of factors considered by our board of directors, our board of directors did not find it practicable to quantify or otherwise assign relative weights to the foregoing factors. Our board of directors approved and recommends the merger based upon the totality of the information presented to and considered by it.

**Recommendation of the Company’s Board of Directors**

After careful consideration, the Company’s board of directors:

- has determined that the merger and the merger agreement are advisable, fair to and in the best interests of the Company’s stockholders;

· has approved the merger agreement; and

· recommends that the Company's stockholders vote "FOR" the adoption of the merger agreement.

**Opinion of The Blackstone Group L.P.**

16

Blackstone has acted as our financial advisor in connection with the proposed merger. We selected Blackstone based on Blackstone's experience, reputation and familiarity with the Company's business. Blackstone is an internationally recognized investment banking firm and is continually engaged in the valuation of businesses and their securities in connection with mergers and acquisitions, leveraged buyouts and valuations for corporate and other purposes. Our board of directors engaged Blackstone to render an opinion as to the fairness, from a financial point of view as of September 22, 2006, of the merger consideration to be received by the holders of shares of Talk America common stock.

At the September 22, 2006 meeting at which our board of directors considered the proposed merger, Blackstone delivered an oral opinion to our board of directors, which was subsequently confirmed in writing, to the effect that, as of such date and based upon and subject to the assumptions, qualifications and limitations set forth therein, the $8.10 in cash per share of common stock to be received by the holders of our common stock in the proposed merger was fair to such holders from a financial point of view.

**The full text of Blackstone’s opinion, dated September 22, 2006, to our board of directors, is attached as Annex B to this proxy statement and is incorporated herein by reference. The opinion outlines the procedures followed, assumptions made, matters considered and qualifications and limitations on the review undertaken by Blackstone in rendering its opinion. The description of the opinion set forth below is qualified in its entirety by reference to the opinion. We urge you to read the opinion carefully and in its entirety in connection with your consideration of the proposed merger.**

**Blackstone’s opinion speaks only as of the date of the opinion. The opinion is directed to our board of directors and addresses only the fairness, from a financial point of view, to our stockholders of the $8.10 in cash per share of common stock to be paid to the holders of our common stock by Cavalier Telephone Corporation in the proposed merger. It does not address any other aspect of the proposed merger or the underlying business decision of the Company to proceed with the proposed merger and is not a recommendation to any of our stockholders as to how a stockholder should vote in connection with the proposed merger or any other matter.**

In arriving at its opinion, Blackstone, among other things:

- reviewed certain publicly available information concerning our business and financial condition that it believed to be relevant to its inquiry;
- reviewed certain internal information concerning our business, financial condition, and operations that it believed to be relevant to its inquiry;
- reviewed certain internal financial analyses, estimates and forecasts relating to the Company prepared and furnished to Blackstone by our management, including our 2006 budget and long-term business plan;
- reviewed the reported prices and trading activity for our common stock;
- reviewed an unexecuted draft of the merger agreement dated September 21, 2006;
- held discussions with members of our senior management concerning our business, operating environment, financial condition, prospects and strategic objectives;
- reviewed publicly available financial and stock market data with respect to certain other competitive local exchange carriers (“CLECs”) that are in businesses that Blackstone believed to be generally comparable to those of the Company;

- reviewed the financial terms of certain recent CLEC business combinations that Blackstone believed to be comparable;

- reviewed the premiums over trading prices paid in recent acquisitions of publicly-traded companies that Blackstone believed to be comparable;

17

- performed a discounted cash flow analysis of the Company based on our business plan referred to above;
- performed a leveraged buyout analysis of the Company based on our business plan referred to above; and
- conducted such other financial studies, analyses, and investigations, and considered such other information as Blackstone deemed necessary or appropriate.

In preparing its opinion, with the consent of our board of directors, Blackstone relied, without assuming responsibility for independent verification, upon the accuracy and completeness of all financial and other information that was available from public sources and all projections and other information provided to it by the Company or otherwise reviewed by Blackstone. Blackstone assumed that the financial projections prepared by the Company and the assumptions underlying those projections, including the amounts and the timing of all financial and other performance data, were reasonably prepared and represented our management's best estimates as of the date of their preparation. Blackstone expressed no view as to such analyses or forecasts or the assumptions on which they were based. Blackstone further relied upon the assurances of our management that they were not aware of any facts that would make the information and projections provided by them inaccurate, incomplete or misleading.

Blackstone was not asked to undertake, and did not undertake, an independent verification of any information, and Blackstone did not assume any responsibility or liability for the accuracy or completeness thereof. Blackstone did not conduct a physical inspection of any of our properties or assets. Blackstone also did not make an independent evaluation or appraisal of our specific assets or liabilities, nor was it furnished with any such evaluations or appraisals.

Blackstone assumed that the definitive merger agreement would not differ in any material respects from the draft thereof furnished to it. Blackstone also assumed that the proposed merger would be consummated in accordance with the merger agreement, without waiver, amendment or modification of any material terms, conditions, or agreements therein and that at least 30,508,638 shares of our common stock would be outstanding at the effective time of the merger.

Blackstone's opinion did not address the relative merits of the proposed merger as compared to other business strategies or opportunities that might be available to the Company, the effect of any other arrangement in which we might engage or our underlying business decision to effect the proposed merger, nor does Blackstone's opinion constitute a recommendation to any of our stockholders as to how such stockholder should vote or act with respect to the proposed merger or any other matter.

The Blackstone opinion was necessarily based upon market, economic, financial and other conditions as they existed and could be evaluated as of the date of the opinion only. Blackstone assumed no responsibility to update or revise its opinion based on circumstances or events occurring after the date of the opinion.

In preparing its opinion to our board of directors, Blackstone performed a variety of financial and comparative analyses, including those described below. The preparation of a fairness opinion is complex and is not readily susceptible to partial analysis or summary description. Accordingly, Blackstone believes that its analyses must be considered as a whole and that selecting portions of its analyses and factors, or the narrative description of the analyses, could create a misleading or incomplete view of the processes underlying its analyses and opinion.

No company, transaction or business used in Blackstone's analyses as a comparison is directly comparable to the Company or the proposed merger, and an evaluation of the results of those analyses is not entirely mathematical. Rather, the analyses involve complex considerations and judgments concerning differences in financial and operating characteristics of the comparable companies, business segments or transactions and other factors that could affect the proposed merger or the other values of the companies, business segments or transactions being analyzed.

The estimates contained in Blackstone's analyses and the ranges of valuations resulting from any particular analysis are not necessarily indicative of actual values or predictive of future results or values, which may be significantly more or less favorable than those suggested by the analyses. The analyses do not purport to be appraisals and do not necessarily reflect the prices at which businesses actually may be sold, and such estimates are inherently subject to uncertainty.

Blackstone's opinion and financial analyses were among many factors considered by our board of directors in its evaluation of the proposed merger and should not be viewed as determinative of the views of our board of directors or management with respect to the proposed merger or the $8.10 in cash per share of common stock to be paid to the holders of our common stock.

***Summary of Financial Analyses.***

The following is a summary of the material financial analyses underlying Blackstone's opinion. The financial analyses summarized below include information presented in tabular format. In order to fully understand Blackstone's financial analyses, the tables must be read together with the text of each summary. Considering the data set forth in the tables below without considering the full narrative description of the financial analyses, including the methodologies and assumptions underlying the analyses, could create a misleading or incomplete view of Blackstone's financial analyses. Predictions of results of operations, cash flows and EBITDA for 2006 and subsequent years set forth in the following analyses are not guaranteed, involve risks and uncertainties and may not accurately predict future results of the Company. These predictions may be affected by the various factors described above in the section called ''Cautionary Statement Concerning Forward-Looking Information.''

*Comparable Trading Multiples*

Blackstone's Comparable Trading Multiples valuation included (i) a discounted cash flow valuation of the Company's off-net business (i.e., not served by our own networking facilities) and (ii) a multiples-based analysis of the Company's on-net business (i.e., served by our owned networking facilities) to determine an indicative valuation range for the Company's common stock. Publicly traded CLECs, which each primarily provide on-net services to commercial customers, while comparable to the Company's on-net business, do not have any significant residential businesses nor do they have operations or financial characteristics comparable to the Company's off-net business, which has high revenue churn and limited capital requirements. Blackstone was provided with a 2006 budget and long-term business plan segmented between the Company's on-net and off-net business with projections as follows:

| *($ in millions)* | **2006E** | **2007E** | **2008E** | **2009E** | **2010E** |
|---|---|---|---|---|---|
| Revenues | | | | | |
| On-Net | $ 249.9 | $ 264.9 | $ 302.8 | $ 340.1 | $ 372.1 |
| Off-Net | 187.6 | 105.7 | 70.3 | 51.0 | 40.5 |
| Total | $ 437.6 | $ 370.6 | $ 373.1 | $ 391.1 | $ 412.6 |
| | | | | | |
| EBITDA | | | | | |
| On-Net | $ 1.5 | $ 11.6 | $ 30.5 | $ 45.4 | $ 60.6 |
| Off-Net | 53.7 | 30.9 | 21.7 | 16.6 | 13.7 |
| Total | $ 55.2 | $ 42.5 | $ 52.1 | $ 62.0 | $ 74.3 |
| | | | | | |
| Capital Expenditures / Capitalized Software Costs | | | | | |
| On-Net | $ 29.9 | $ 21.9 | $ 22.1 | $ 22.1 | $ 22.1 |
| Off-Net | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Total | $ 29.9 | $ 21.9 | $ 22.1 | $ 22.1 | $ 22.1 |

Blackstone performed a discounted cash flow analysis of the present value of the unlevered cash flows that the Company's off-net business is estimated to generate over the six months ending December 31, 2006 and in the fiscal years 2007 through 2010 as per our management projections. For this analysis, Blackstone applied perpetual growth rates ranging from negative 15% to negative 25% to the Company's 2010 projected off-net unlevered cash flows. The projected unlevered cash flows were then discounted to present value using a weighted average cost of capital, or WACC, of 14.0% to 15.0% (see Discounted Cash Flow for detail). Blackstone also calculated cash taxes at 40% on an unlevered normalized basis and utilized a $26 million initial net operating loss carryforward through 2010, with additional net operating losses created over the projection period, in its computation of cash taxes. The sum of (i) the net present value of the Company's off-net unlevered cash flows from July 1, 2006 to December 31, 2010 at a WACC of 14.0% to 15.0% and (ii) the net present value of the Company's off-net terminal value based on a perpetual growth rate of negative 15% to negative 25% and a WACC of 14.0% to 15.0% was used by Blackstone to derive an implied total enterprise value of the Company's off-net business of $72.0 million to $77.6 million.

To determine an implied valuation range for the Company's on-net business, Blackstone reviewed and analyzed certain public market trading data for publicly traded CLECs that it deemed comparable to the on-net business of the Company, using publicly available information including company filings, Wall Street equity research and the Institutional Brokerage Estimate System (a data service that compiles estimates issued by securities analysts). The peer group consisted of the following publicly traded CLECs with total enterprise values (equity market capitalization plus total debt, preferred stock and minority interests less cash and unconsolidated equity investments) ranging from approximately $352 million to $3,760 million based on the closing stock prices as of September 20, 2006:

*CLECs:*

· Broadwing Corporation

· Cbeyond Communications, Inc.

· Covad Communications Group, Inc.

· Eschelon Telecom, Inc.

· ITC^DeltaCom, Inc.

· Time Warner Telecom Inc.

· US LEC Corp.

· XO Holdings, Inc.

The table below sets forth the implied range of trading multiples and mean trading multiples for the peer group and the mean trading multiples for a subset of the peer group (consisting of US LEC, Eschelon Telecom and ITC^Deltacom, which it deemed most comparable to the Company's on-net business model) as of September 20, 2006. With respect to the peer group, Blackstone calculated the implied multiples of the enterprise value to the estimated 2006 and 2007 revenue, EBITDA and EBITDA less capital expenditures.

| | **Total Enterprise Value as a Multiple of** | | | |
|---|---|---|---|---|
| | **Low** | **High** | **Mean** | **Mean CLEC, ESCH, ITCD** |
| 2006E Revenues | 0.8x | 3.7x | 1.7x | 1.1x |
| 2007E Revenues | 0.8x | 3.5x | 1.5x | 1.0x |
| 2006E EBITDA | 6.2x | 23.2x | 12.5x | 6.7x |
| 2007E EBITDA | 4.8x | 17.5x | 9.9x | 5.8x |
| 2006E EBITDA — Capital Expenditures | 13.4x | 18.8x | 16.0x | 14.6x |
| 2007E EBITDA — Capital Expenditures | 11.4x | 23.0x | 15.1x | 12.8x |

In determining the reference range, Blackstone noted our high level of residential revenues (62% of second quarter 2006 revenues) relative to trading comparables, the competitive challenges in the residential segment and our management's projection of negative free cash flow in our on-net business until 2008. Based on the foregoing, Blackstone determined an enterprise value-to-estimated 2007 EBITDA multiple reference range of 5.0x to 5.8x and applied such range to our projected 2007 on-net EBITDA (based on our management projections) to calculate an enterprise value range for the Company's on-net business of $58.0 million to $66.9 million. Blackstone then added this implied on-net valuation to the off-net discounted cash flow valuation to derive an implied total enterprise valuation range of $130.0 million to $144.4 million. Blackstone then subtracted our net cash outstanding as of June 30, 2006, as publicly disclosed by us, from these enterprise value ranges and divided those amounts by the number of fully diluted shares of our common stock outstanding, based on information received by Blackstone from our management team, to derive an implied per share valuation range for our common stock of $5.16 to $5.64, as compared to the consideration per common share of $8.10 to be paid in the proposed merger.

*Precedent Transaction*

Recent CLEC merger transactions have involved target companies with predominantly on-net businesses with commercial customer bases that are not comparable to the Company's off-net business. As a result, Blackstone's Precedent Transactions valuation included (i) a discounted cash flow valuation of the Company's off-net business (discussed above) and (ii) a multiples-based analysis of the Company's on-net business to determine an indicative valuation range for the Company's common stock.

Blackstone reviewed and analyzed the following twelve merger transactions announced from March 8, 2004 through August 14, 2006 involving target CLECs (the ''Comparable Transactions''), using publicly available information from company news releases and filings, Wall Street equity research and the Institutional Brokerage Estimate System:

| **Target** | **Acquiror** |
|---|---|
| US LEC Corp. | PAETEC Communications, Inc. |
| Xspedius Communications | Time Warner Telecom Inc. |
| Mpower Communications Corp. | U.S. TelePacific Corp. |
| TelCove, Inc. | Level 3 Communications, Inc. |
| ICG Communications, Inc. | Level 3 Communications, Inc. |
| Conversent Communications, LLC | Choice One Communications Inc. / CTC Communications Corp. |
| Electric Lightwave, Inc. | Integra Telecom, Inc. |
| Oregon Telecom, Inc. | Eschelon Telecom, Inc. |
| LDMI Telecommunications, Inc. | Talk America Holdings, Inc. |
| Lightship Telecom LLC | CTC Communications Corp. |
| Advanced TelCom, Inc. | Eschelon Telecom, Inc. |
| Focal Communications Corporation | Corvis Corporation |

Blackstone calculated the implied multiples of transaction total enterprise value of each comparable target company in the selected transactions described above at announcement to the revenues and EBITDA estimated in the year following announcement. The table below sets forth the implied multiples and implied mean multiples for the target companies in the selected transactions described above.

| | **Transaction Total Enterprise Value as a Multiple of** | | | |
|---|---|---|---|---|
| | **Low** | **High** | **Mean** | **Median** |
| Revenues | 0.4x | 3.2x | 1.4x | 1.2x |
| EBITDA | 5.2x | 11.8x | 7.8x | 7.6x |

In determining the reference range, Blackstone noted our high level of residential revenues relative to targets in precedent transactions, the competitive challenges in our residential segment and our management's projection of negative free cash flow in our on-net business until 2008 relative to the free cash flow generated by targets in precedent transactions. Based on the foregoing, Blackstone determined an enterprise value-to-estimated 2007 EBITDA multiple reference range of 6.5x to 7.6x and applied such range to the projected 2007 EBITDA for the Company's on-net business (based on our management projections) to calculate an enterprise value range for the Company's on-net business of $75.4 million to $88.2 million. Blackstone then added this implied on-net valuation to the off-net discounted cash flow valuation to derive an implied total enterprise valuation range of $147.4 million to $165.7 million. Blackstone then subtracted our net cash outstanding as of June 30, 2006, as publicly disclosed by us, from these enterprise value ranges and divided those amounts by the number of fully diluted shares of our common stock outstanding, based on information received by Blackstone from our management team, to derive an implied per share valuation range for our common stock of $5.73 to $6.34, as compared to the consideration per common share of $8.10 to be paid in the proposed merger.

*Premiums Paid Analysis.*

Blackstone reviewed and analyzed the premiums paid relative to public market pre-announcement trading prices for all completed cash transactions involving a change in control between $100 million and $300 million in size completed since January 1, 2004. Blackstone examined a group of 82 transactions. Blackstone calculated and compared the premiums paid in these transactions based on the value of the per share consideration received in the transaction relative to the closing stock price of each target company one day, one week and one month prior to the announcement of each respective transaction.



---

Blackstone compared the implied average premiums for the selected transactions to the premium to closing prices of our common stock for the corresponding dates implied by the consideration per common share of $8.10 to be paid in the merger. The following table summarizes the results of this analysis:

| | Premium to Market Per Share Price | | |
|---|---|---|---|
| | **Mean** | **Median** | **Talk America / Cavalier** |
| 1 day prior to announcement | 22.4% | 20.6% | 22.4% |
| 1 week prior to announcement | 23.4% | 23.1% | 25.7% |
| 1 month prior to announcement | 25.7% | 23.9% | 37.0% |

Based on the foregoing, Blackstone derived an implied per share valuation range based on a 20% to 30% premium over the Company's 30-day trading average, of $7.09 to $7.68 per share, as compared to the consideration per common share of $8.10 to be paid in the proposed merger.

*Discounted Cash Flow*

Blackstone performed discounted cash flow analyses of the present value of the unlevered cash flows that the Company's on-net business and off-net business is estimated to generate between July 1, 2006 and December 31, 2010, as per our management projections. For the key assumptions and implied valuation range for the discounted cash flow valuation of the off-net business, please see "Comparable Trading Multiples". For the discounted cash flow analysis of the on-net business, Blackstone applied a terminal multiple of 4.5x - 5.5x to our management-projected 2010 on-net EBITDA (implying perpetual unlevered cash flow growth rates ranging from 6.9% to 8.2%). The projected unlevered cash flows were then discounted to present value using a weighted average cost of capital, or WACC, of 14.0% to 15.0% (based on a mean unlevered beta of 1.04 for selected CLEC comparables, and a targeted debt-to-total capitalization ratio of 30%). Unlevered beta is a measure of the volatility in a company's stock market price relative to the broader stock market that is calculated assuming that the company being analyzed has no debt in its capital structure. Blackstone also calculated cash taxes at 40% on an unlevered normalized basis and utilized a $26 million initial net operating loss carryforward through 2010, with additional net operating losses created over the projection period, in its computation of cash taxes. The sum of (i) the net present value of our management-projected on-net unlevered cash flows from July 1, 2006 to December 31, 2010 at a WACC of 14.0% to 15.0% and (ii) the net present value of the Company's terminal value based on a terminal multiple of 4.5x - 5.5x 2010 EBITDA and a WACC of 14.0% to 15.0% was used by Blackstone to derive an implied total enterprise value of the Company's on-net business of $129.9 million to $169.7 million. Blackstone then added these implied on-net valuations to the implied discounted cash flow valuation of our off-net business (discussed above in "Comparable Trading Multiples") to derive an implied total enterprise valuation range of $201.9 million to $247.3 million. Blackstone noted that the net present value of the Company's on-net unlevered cash flows from July 1, 2006 to December 31, 2010 was negative and that over 100% of the implied on-net valuation was attributable to the net present value of our on-net business' terminal value. Blackstone then subtracted our net cash outstanding as of June 30, 2006, as publicly disclosed by us, from these enterprise value ranges and divided those amounts by the number of fully diluted shares of our common stock outstanding, based on information received by Blackstone from our management team, to derive an implied per share valuation range for our common stock of $7.46 to $8.83, as compared to the consideration per common share of $8.10 to be paid in the proposed merger.

*Leveraged Buyout*

Blackstone performed a leveraged buyout analysis of the Company to derive an estimated per share equity valuation range. In performing this analysis, Blackstone analyzed the cash flows related to our operations for the period of January 1, 2007 through December 31, 2010 using our management business plan projections. This analysis assumed (i) a 4-year holding period; (ii) a target internal rate of return ("IRR") of 25%-30%; (iii) leverage capacity of 4.25x our management's projected 2007 on-net EBITDA plus 70% loan-to-value on the discounted cash flow valuation of our off-net business; and (iv) exit assumptions based on a terminal valuation of our management-projected year 2010 on-net EBITDA of 4.5x to 5.5x and implied perpetual growth rates on off-net unlevered free cash flow of negative 15% to negative 25%. Based on these assumptions, the leveraged buyout analysis resulted in an implied equity value per share of common stock that ranged from $6.75 to $7.25, as compared to the consideration per common share of $8.10 to be paid in the proposed merger.

**Miscellaneous.**

Blackstone acted as financial advisor to the Company with respect to the proposed merger. We agreed to pay Blackstone customary fees for its financial advisory services, a significant portion of which are contingent and payable only if the proposed merger is completed. In addition, we agreed to reimburse Blackstone for out-of-pocket expenses and to indemnify and hold harmless Blackstone and its affiliates and their respective partners (both general and limited), members, officers, directors, employees and agents and each other person, if any, controlling Blackstone or any of its affiliates from and against certain liabilities arising out of the performance of such services (including the rendering of its opinion), including certain liabilities under the federal securities laws.

Blackstone has, in the past, provided financial advisory services to the Company and/or our affiliates and may continue to do so. In the ordinary course of their business, affiliates of Blackstone may actively trade in the securities of Talk America for their own account and, accordingly, may at any time hold a long or short position in such securities.

**Financing**

In connection with the merger, the Parent will cause approximately $[ ] million in cash to be paid to the Company's stockholders and holders of the Company's stock options and warrants.

These payments are expected to be funded by a combination of credit facilities provided to the Parent and its subsidiary, CavTel Holdings, LLC or CavTel. In connection with the execution and delivery of the merger agreement, the Parent and CavTel have obtained a commitment letter from Wachovia Bank, National Association and Wachovia Capital Markets, LLC providing for $435 million in credit facilities.

The commitment is conditioned on the merger being consummated by January 31, 2007, and other customary conditions. Wachovia Bank, National Association and Wachovia Capital Markets, LLC have the right to terminate the commitment under certain circumstances, including the occurrence of events which are substantially similar to the events constituting a "material adverse effect" on the Company that are described in "The Merger Agreement — Conditions to the Merger."

The merger agreement does not contain a financing condition to the consummation of the merger or the obligations of the Parent or the Merger Sub. Under the terms of the merger agreement, the Parent has represented to us that it will have sufficient funds available to permit the Parent to perform all of its obligations under the merger agreement and to consummate the merger.

**Interests of the Company's Directors and Executive Officers in the Merger**

Some of our executive officers and members of our board of directors have financial interests in the merger that are in addition to, or different from, their interests as our stockholders generally. Our board of directors was aware of these interests and considered them, among other matters, in approving the merger agreement.

***Company Stock Options and Other Equity Awards***

As of September 29, 2006, there were approximately 2,940,000 shares of our common stock subject to outstanding stock options granted to our executive officers and directors under our stock option plans, of which options to purchase approximately 647,300 shares had an exercise price less than the merger consideration price of $8.10. Under the terms of the merger agreement, any outstanding stock options that remain outstanding and unexercised as of the effective time of the merger will be canceled, and the holder of each stock option that has an exercise price of less than $8.10 will receive from the surviving corporation as soon as practicable thereafter a cash payment, less any applicable withholding taxes, equal to the product of:

- the number of shares of our common stock subject to each stock option as of the effective time of the merger, multiplied by
    - the excess of $8.10 over the exercise price per share of common stock subject to such stock option.

The following table summarizes (i) the stock options with exercise prices of less than $8.10 per share held by each of our executive officers and directors as of September 29, 2006 (with an assumption that all then unvested stock options will be vested at and as a consequence of the merger) and (ii) the consideration that each of them will receive pursuant to the merger agreement in connection with the cancellation of their stock options:

| | No. of Shares Underlying Stock Options(1) | | | |
|---|---|---|---|---|
| | Number of Shares Underlying Stock Options with exercise price less than the $8.10 | Number of Shares Underlying Stock Options with exercise price equal to or higher than the $8.10 | Weighted Average Exercise Price of Stock Options with exercise price less than the $8.10 | Resulting Consideration for Stock Options with exercise price less than the $8.10 |
| Gabriel Battista *Chairman of the Board of Directors* | 183,821 | 457,844 | $3.56 | $835,205 |
| Mark Fowler *Director* | 25,000 | 50,000 | $4.90 | $80,100 |
| Robert Korzeniewski *Director* | 15,000 | 30,000 | $7.36 | $11,100 |
| Ronald Thoma *Director* | 25,000 | 40,000 | $4.90 | $80,100 |
| Edward B. Meyercord, III *Chief Executive Officer, President and Director* | 100,000 | 616,666 | $3.77 | $433,500 |
| Warren Brasselle *Executive Vice President - Network Operations* | 28,333 | 160,000 | $1.53 | $186,148 |
| Jeffrey Earhart *Executive Vice President - Customer Operations* | 31,000 | 160,000 | $6.00 | $65,100 |
| Aloysius T. Lawn, IV *Executive Vice President - General Counsel and Secretary* | 105,833 | 176,666 | $3.47 | $490,449 |
| Timothy W. Leonard *Chief Information Officer* | 31,666 | 143,333 | $3.23 | $154,146 |
| Patrick O'Leary *Executive Vice President - Business Services* | -- | 75,000 | N/A | $0 |
| Thomas Walsh *Senior Vice President - Finance and Treasurer* | 1,667 | 148,333 | $1.53 | $10,952 |
| Paul Walker *Senior Vice President - Marketing* | 50,000 | 50,000 | $6.38 | $86,000 |
| Mark Wayne | | | | |

| | | | | |
|---|---|---|---|---|
| *Senior Vice President - Business Sales* | -- | 50,000 | N/A | $0 |
| David G. Zahka<br>*Chief Financial Officer* | 50,000 | 135,000 | $1.20 | $345,000 |

**(1) Assumes that all options will be vested as of the closing date of the merger.**

**Compensation Under Existing Employment Agreements**

We have entered into various employment agreements with our executive officers pursuant to which payments may be made in connection with the merger as described below.

24

*Edward B. Meyercord, III, Aloysius T. Lawn, IV, Warren Brasselle, Jeffrey Earhart, Timothy W. Leonard, Patrick O'Leary, David G. Zahka, Thomas Walsh and Mark Wayne.* The Company is party to employment agreements with each of Messrs. Meyercord, Lawn, Brasselle, Earhart, Leonard, O'Leary, Zahka, Walsh and Wayne, each of which agreements provides for immediate vesting of options in event of a "change of control" (as defined in the agreements) of us and, except for Mr. O'Leary's agreement, provides for severance benefits in the event employment is terminated by us without cause or by the employee for "good reason" prior to the end of the term and for a certain period beyond the end of the term in the event of a "change of control." These severance benefits generally include the payment of an amount equal to one year's (two year's in the case of Mr. Meyercord) base salary plus all bonus amounts due such executive at the time of termination, a lump sum amount equal to one year (two years in the case of Mr. Meyercord) base salary plus an amount equal to the average annual incentive bonus earned by the executive during the past four fiscal years preceding the date of change of control, or if the executive was not an officer during any or all of such prior four fiscal year, the average of the incentives received during the fiscal year when the executive was such an officer, and the continuation of various employee benefits for one year (two year's in the case of Mr. Meyercord). Based upon their current levels of compensation, if the employment of Messrs. Meyercord, Lawn, Brasselle, Earhart, Leonard, Zahka, Walsh and Wayne were terminated upon the effective time of the merger, they would be entitled to receive severance payments of approximately $1.4 million, $489,775, $445,250, $445,250, $445,250, $445,250, $341,300 and $279,135, respectively, or approximately $4,291,000 in the aggregate.

The merger agreement permits the Company, on the closing date of the merger, to make, and the Company proposes to make, lump sum payments in the amounts set forth above to the Company executive officers who are party to such employment agreements in the full amount of the severance payment that they would be entitled to receive upon a "change of control," which the merger would constitute, and termination of employment, whether or not such employment will be terminated or the employee otherwise would have the opportunity to terminate with good reason.

Although Cavalier has not finalized any agreements with any executive officers of Talk America, Cavalier expects to enter into employment agreements with each of Messrs. Meyercord, Braselle, Earhart, Leonard and Wayne. Mr. Meyercord would serve as Chief Executive Officer, reporting to Mr. Evans, who would become Cavalier's Executive Chairman of its board of directors. Each of Messrs. Braselle, Earhart, Leonard and Wayne would serve in substantially the same capacities for Cavalier as each has been serving for Talk America. Cavalier expects the terms of each of these agreements to be no more favorable to the respective executive officer than the terms of such executive officer's existing employment agreement with Talk America. Cavalier also expects to grant each of these executive officers options for Cavalier common stock. These expected terms are current expectations and constitute forward-looking statements. Neither Cavalier nor any of Messrs. Meyercord, Braselle, Earhart, Leonard nor Wayne is obligated to enter into an employment agreement, and, if the parties enter into employment agreements, the agreements may contain terms that differ materially from those described above.

***Bonus Payments***

Under the terms of the merger agreement, our board of directors is permitted, in its sole discretion, to award and pay bonuses to our employees, including our executive officers, at or prior to the closing date of the merger, in an aggregate amount up to $2.5 million; while our board has generally indicated that it expects to award some discretionary bonuses, it has not yet made any decision as to which, if any, persons would be awarded bonuses or any amounts thereof

***Indemnification and Insurance***

The Parent and the surviving corporation have agreed to indemnify for a period of six years, to the same extent as provided in our amended and restated certificate of incorporation, bylaws or any other applicable contract in effect on September 22, 2006, each of our present and former directors and officers against all expenses, losses and liabilities incurred in connection with any claim, proceeding or investigation arising out of any act or omission in their capacity as an officer or director occurring on or before the effective time of the merger.

The merger agreement requires that the surviving corporation obtain fully prepaid tail directors' and officers' insurance policies in an amount and scope not materially less favorable than those in the Company's existing policies (and which provides for a claims period of at least six years from the effective time of the merger for claims arising from facts or events that occurred on or prior to the effective time).

The obligations described above regarding directors' and officers' indemnification and insurance must be assumed by any successor entity to the Parent or the surviving corporation as a result of any consolidation, merger or transfer of all or substantially all properties and assets.

**Rights Agreement**

Immediately prior to the execution of the merger agreement, we amended our rights agreement on September 22, 2006 (the date the merger agreement was executed) to exempt the execution of the merger agreement and the consummation of the transactions contemplated by the merger agreement in accordance with the terms thereof. In particular, our amendment provides that neither the Parent, the Merger Sub nor any of their affiliates will be deemed to be an "acquiring person" (as such term is defined in the rights agreement) solely by virtue of the execution and delivery of the merger agreement or the consummation of the transactions contemplated by the merger agreement.

**Material U.S. Federal Income Tax Consequences**

The following is a general discussion of certain material U.S. federal income tax consequences of the merger to U.S. holders of our common stock. We base this summary on the provisions of the Internal Revenue Code of 1986, as amended (the "Code"), as currently in effect, applicable current and proposed U.S. Treasury Regulations, judicial authority, and administrative rulings and practice, all of which are subject to change, possibly on a retroactive basis. There can be no assurance that the Internal Revenue Service or a court of law will agree with the positions described in this proxy statement.

For purposes of this discussion, we use the term "U.S. holder" to mean a beneficial owner of Talk America common stock that is:

- a citizen or individual resident of the United States for U.S. federal income tax purposes;
- a corporation, or other entity taxable as a corporation for U.S. federal income tax purposes, created or organized in or under the laws of the United States, any State thereof or the District of Columbia;
- a trust if it (i) is subject to the primary supervision of a court within the United States and one or more U.S. persons (as described in Section 7701(a)(30) of the Code) have the authority to control all substantial decisions of the trust or (ii) has a valid election in effect under applicable U.S. Treasury Regulations to be treated as a U.S. person; or
- an estate the income of which is subject to U.S. federal income tax regardless of its source.

The U.S. federal income taxes of a partner in a partnership holding our common stock will depend on the status of the partner and the activities of the partnership. Partners in a partnership holding shares of our common stock should consult their own tax advisors.

This discussion assumes that you hold the shares of our common stock as a capital asset within the meaning of Section 1221 of the Code (generally, property held for investment). This discussion is limited to the U.S. federal income tax issues addressed herein. This discussion does not address all aspects of U.S. federal income tax that may be relevant to you in light of your particular circumstances, or that may apply to you if you are subject to special treatment under the U.S. federal income tax laws (including, for example, if you are a stockholder subject to the alternative minimum tax, an insurance company, dealer in securities or foreign currencies, tax-exempt organization, financial institution, mutual fund, partnership or other pass through entity for U.S. federal income tax purposes, stockholder who holds shares of our common stock as part of a hedge, straddle, constructive sale or conversion transaction, a stockholder that directly, indirectly or constructively owns at least 50% of the stock (by vote or value) of both the Company and the Parent, or stockholder who acquired your shares of our common stock through the exercise of employee stock options or other compensation arrangements). In addition, the discussion does not address any tax considerations under state, local or foreign laws or U.S. federal laws other than those pertaining to the U.S. federal income tax. This discussion does not address the U.S. federal income tax consequences to a stockholder that, for U.S. federal income tax purposes, is a non-resident alien individual, a foreign corporation, a foreign partnership or a foreign trust or estate. We urge you to consult your own tax advisor to determine the particular tax consequences to you, including the application and effect of any state, local or foreign income and other tax laws, of the receipt of cash in exchange for our common stock pursuant to the merger.

The receipt of cash in the merger by U.S. holders of our common stock will be a taxable transaction for U.S. federal income tax purposes. In general, for U.S. federal income tax purposes, a U.S. holder of our common stock will recognize gain or loss equal to the difference between:

26

· the amount of cash received in exchange for such common stock; and

· the U.S. holder's adjusted tax basis in such common stock.

Such gain or loss generally will be capital gain or loss and will be long-term capital gain or loss if the holding period in our common stock surrendered in the merger is greater than one year as of the date of the merger. The deductibility of a capital loss recognized on the exchange is subject to limitations under the Code. Certain U.S. holders, including individuals, are eligible for preferential rates of U.S. federal income tax in respect of long-term capital gains. If you acquired different blocks of our common stock at different times or different prices, you must determine your adjusted tax basis and holding period separately with respect to each block of our common stock.

Under the Code, you may be subject to information reporting on the cash received in the merger. Backup withholding will also apply (currently at a rate of 28%) with respect to the amount of cash received in the merger, unless you provide proof of an applicable exemption or a correct taxpayer identification number, and otherwise comply with the applicable requirements of the backup withholding rules. Backup withholding is not an additional tax and any amounts withheld under the backup withholding rules may be refunded or credited against your U.S. federal income tax liability, if any, provided that you furnish the required information to the Internal Revenue Service in a timely manner.

**Regulatory Approvals**

The Hart-Scott-Rodino Antitrust Improvements Act of 1976 and related rules provide that transactions such as the merger may not be completed until certain information has been submitted to the Federal Trade Commission and the Antitrust Division of the U.S. Department of Justice and specified waiting period requirements have been satisfied. On [ ], 2006, the Company and the Parent each filed a Notification and Report Form with the Antitrust Division and the Federal Trade Commission and requested an early termination of the waiting period. If the early termination is not granted and a request for additional information by the relevant antitrust authorities is not made, the waiting period will expire at 11:59 p.m. on [ ], 2006.

Certain of the Company's subsidiaries provide communications services that are regulated by the FCC and/or State PUCs. As providers of such services, those subsidiaries hold authorizations issued by the FCC and State PUCs. Permission from or notices to many of these regulatory agencies is required to transfer control of the subsidiaries and therefore to complete the transfer of control of the Company.

Under the Communications Act of 1934, as amended, prior FCC approval is required for the transfer of control to the Parent of the Company and those subsidiaries of the Company that hold FCC licenses and authorizations. The FCC must determine whether the Parent is qualified to control such licenses and authorizations and whether the transfer is consistent with the public interest. The Company and the Parent filed a transfer of control application with the FCC on [ ], 2006.

Certain subsidiaries of the Company also hold certificates and authorizations issued by State PUCs in all U.S. states (except Alaska) and the District of Columbia where they provide intrastate telecommunications services. Many of the State PUCs in each of the states where Company subsidiaries operate must either approve the transactions contemplated by the merger agreement or require that formal notice of the transactions be provided to them. As of [ ], 2006, the Company and the Parent had filed the necessary applications and notices with these State PUCs.

## THE MERGER AGREEMENT

The summary of the material terms of the merger agreement below and elsewhere in this proxy statement is qualified in its entirety by reference to the merger agreement, a copy of which is attached to this proxy statement as Annex A and which we incorporate by reference into this document. This summary may not contain all of the information about the merger agreement that is important to you. We encourage you to read carefully the merger agreement in its entirety. The merger agreement has been included to provide you with information regarding its terms. It is not intended to provide any other factual information about the Company or the Parent. The merger agreement contains representations and warranties that the parties to the merger agreement made to and solely for the benefit of each other, and the assertions embodied in such representations and warranties are qualified by information contained in confidential disclosures that the parties exchanged in connection with signing the merger agreement. These representations and warranties may have been made for the purposes of allocating contractual risk between the parties to the merger agreement instead of establishing these matters as facts, and may be subject to standards of materiality applicable to the contracting parties that differ from those applicable to investors. Accordingly, you should not rely on such representations and warranties as characterizations of the actual state of facts or circumstances, since they were only made as of the date of the merger agreement and are modified in important part by the underlying disclosures.

**Effective Time**

The merger will become effective upon the filing of a certificate of merger with the Secretary of State of the State of Delaware or at such later time as may be stated by the parties in such certificate of merger. The filing of the certificate of merger will occur at the closing, which will take place two business days after satisfaction or waiver of the conditions to the closing of the merger set forth in the merger agreement and described in this proxy statement, or at such other date and time as is agreed upon by the Parent and the Company.

**Structure**

At the effective time of the merger, the Merger Sub will merge with and into the Company. The Company will survive the merger and continue to exist after the merger as an indirectly, wholly owned subsidiary of the Parent. All of the Company's and the Merger Sub's properties, assets, rights, privileges, powers and franchises, and all of their debts, liabilities, obligations and duties will become those of the surviving corporation. Following the completion of the merger, we expect that our common stock will be delisted from Nasdaq, deregistered under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and no longer publicly traded.

**Treatment of the Company's Common Stock, Options and Warrants**

***Company Common Stock***

At the effective time of the merger, each share of our common stock issued and outstanding immediately prior to the effective time of the merger will automatically be canceled and converted into the right to receive $8.10 in cash, without interest, other than Company common stock:

· held in the Company's treasury immediately prior to the effective time of the merger;

· held by any wholly owned subsidiary of the Company immediately prior to the effective time of the merger; and

· as to which the Company's stockholders demand appraisal in compliance with Delaware law.

***Company Stock Options***

As of the effective time of the merger, each option, issued and outstanding immediately prior to the effective time, to acquire our common stock will be canceled, and the holder of each stock option that has an exercise price of less than $8.10 will receive from the surviving corporation as soon as practicable after the effective time a cash payment, less any applicable withholding taxes, equal to the product of:

· the number of shares of our common stock subject to each stock option, as of the effective time of the merger, multiplied by

· the excess of $8.10 over the exercise price per share of common stock subject to such stock option.

As of the effective time of the merger, the Company's stock option plans will terminate and each stock option granted thereunder that is outstanding and unexercised will be cancelled.

***Company Warrants***

As of the effective time of the merger, each outstanding warrant to acquire our common stock will be canceled. While the merger agreement also provides that each outstanding warrant that has an exercise price of less than $8.10 would be entitled to payments determined in the same manner as are the payments in respect of outstanding options, there are no outstanding warrants that have an exercise price of less than $8.10, so no amounts will be payable in respect of warrants upon the merger.

**Exchange and Payment Procedures**

At the closing of the merger, the Parent will deposit an amount of cash sufficient to pay the merger consideration to holders of shares of our common stock with a financial institution (the “paying agent”) reasonably acceptable to us. Promptly following the effective time of the merger, the surviving corporation will or will cause the paying agent to mail a letter of transmittal and instructions to each holder of certificates evidencing shares of Company common stock. The letter of transmittal and instructions will tell you how to surrender your Company common stock certificates in exchange for the aggregate consideration for such shares of common stock.

You should not return your stock certificates with the enclosed proxy card, and you should not forward your stock certificates to the paying agent without a letter of transmittal.

You will not be entitled to receive the merger consideration until you surrender your Company common stock to the paying agent, together with a duly completed and executed letter of transmittal and any other documents as the paying agent may reasonably require. The merger consideration may be paid to a person other than the person in whose name the corresponding certificate is registered if the certificate is properly endorsed or is otherwise in the proper form for transfer. In addition, the person requesting payment must either pay any applicable stock transfer taxes or establish to the reasonable satisfaction of the surviving corporation that such stock transfer taxes have been paid or are not applicable.

No interest will be paid or will accrue on the cash payable upon surrender of the certificates. Each of the paying agent, the surviving corporation and the Parent will be entitled to deduct and withhold any applicable taxes from the merger consideration.

At the effective time of the merger, our share transfer books will be closed, and there will be no further registration of transfers of outstanding shares of our common stock, warrants or options, as the case may be. If, after the effective time of the merger, certificates are presented to the surviving corporation or the paying agent for transfer or any other reason, they will be canceled and exchanged for the consideration otherwise payable pursuant to the merger agreement.

None of the Merger Sub, the Parent or the surviving corporation will be liable to any person for any cash delivered to a public official pursuant to any applicable abandoned property, escheat or similar law. Any portion of the merger consideration deposited with the paying agent that remains undistributed to the holders of certificates evidencing shares of our common stock for one year after the effective time of the merger will be delivered to the surviving corporation, in its sole discretion. Holders of certificates who have not surrendered their certificates within one year after the effective time of the merger may only look to the surviving corporation for the payment of the applicable consideration.

If you have lost a certificate, or if it has been stolen or destroyed, then you will be required to make an affidavit of that fact before you will be entitled to receive the consideration applicable to such certificate. In addition, if required by the surviving corporation, you will have to post a bond in a reasonable amount determined by the surviving corporation indemnifying the surviving corporation against any claims made against it with respect to the lost, stolen or destroyed certificate.

**Certificate of Incorporation and Bylaws**

The certificate of incorporation of the Merger Sub, as in effect immediately prior to the effective time, will be the certificate of incorporation of the surviving corporation until thereafter amended as provided by law and such certificate of incorporation. In addition, the by-laws of the Merger Sub, as in effect immediately prior to the effective time, will be the by-laws of the surviving corporation, until thereafter amended as provided by-laws and such by-laws.

**Directors and Officers**

29

The directors and officers of the Merger Sub immediately prior to the effective time will, from and after the effective time, be the directors and officers, respectively, of the surviving corporation, each to hold office until his or her respective successors are duly elected or appointed and qualified or until their earlier death, resignation or removal in accordance with the certificate of incorporation and by-laws of the surviving corporation.

**Representations and Warranties**

We make customary representations and warranties in the merger agreement that are subject, in some cases, to specified exceptions and qualifications. Our representations and warranties relate to, among other things:

- our and our subsidiaries' due organization, good standing and corporate power to operate our businesses;
- our corporate power and authority to enter into the merger agreement and to consummate the transactions contemplated by the merger agreement;
- unanimous determination of our board of directors that the merger agreement and merger are fair to and in the best interests of the Company and our stockholders;
- our capitalization;
- the absence of any violation of or conflict with our organizational documents, applicable law or certain agreements as a result of entering into the merger agreement and consummating the merger, except those that have been disclosed to the parent;
- the required filing, consents and approvals of governmental entities as a result of the merger, except those that, individually or in the aggregate, the failure to obtain do not or would not reasonably be expected to result in a material difference;
- our SEC filings since January 1, 2003 and the financial statements contained therein;
- our compliance with the Sarbanes-Oxley Act of 2002 and its related rules;
- the absence of liabilities, with certain exceptions;
- the accuracy and completeness of information supplied by us in this proxy statement;
- no material adverse effect since December 31, 2005;
- real property owned and leased by us, title to assets, and all switches, switch locations and certain network facility information;
- our material contracts;
- environmental matters;
- the absence of undisclosed litigation or outstanding court orders against us other than those that, individually or in the aggregate, do not or would not reasonably be expected to result in a material difference;
- our possession of all licenses and permits necessary to operate our properties and carry on our business, other than those for which our failure to hold such licenses or permits, individually or in the aggregate, do not and would not reasonably be expected to result in a material difference;

- our compliance with all applicable laws other than those disclosed to the Parent;

- our intellectual property;

30

- tax matters;
- employment and labor matters affecting us, including matters relating to our employee benefit plans;
- the absence of undisclosed interested party transactions between January 1, 2006 and the date of the merger agreement;
- the absence of undisclosed broker's fees;
- our insurance policies;
- our relationship with our suppliers;
- the inapplicability of state takeover statutes to the merger;
- the receipt by us of a fairness opinion from Blackstone; and
- the inapplicability of the rights agreement to the merger agreement, the merger and the transactions contemplated by the merger agreement.

The merger agreement also contains customary representations and warranties made by the Parent and the Merger Sub that are subject, in some cases, to specified exceptions and qualifications. The representations and warranties relate to, among other things:

- the Parent's and the Merger Sub's due organization, good standing and corporate power to operate their businesses;
- the Parent's and the Merger Sub's corporate power and authority to enter into the merger agreement and to consummate the transactions contemplated by the merger agreement;
- the absence of any violation of or conflict with the organizational documents of the Parent and the Merger Sub, applicable law or certain agreements as a result of entering into the merger agreement and consummating the merger, except where any such violation or conflict, individually or in the aggregate, would not reasonably be expected to prevent or materially delay the consummation of the merger;
- required filings, consents and approvals of governmental entities as a result of the merger, except those that the failure to obtain, individually or in the aggregate, would not reasonably be expected to prevent or materially delay consummation of the merger;
- the accuracy and completeness of information supplied by the Parent and the Merger Sub in this proxy statement;
- the absence of undisclosed broker's fees;
- the absence of litigation or pending litigation against the Parent or the Merger Sub that individually or in the aggregate, would reasonably be expected to impair the ability of the Parent or Merger Sub to perform its obligations under the merger agreement or prevent or materially delay consummation of the merger;
- the operations of the Merger Sub; and
- the Parent having sufficient funds to consummate the transactions contemplated by the merger agreement and to perform all of its obligations under the merger agreement.

**Conduct of Our Business Pending the Merger**

31

Under the merger agreement, we have that, subject to certain exceptions, between execution of the Merger Agreement and the completion of the merger we and our subsidiaries will:

· conduct our business only in the ordinary course of business consistent with past practice and in compliance in all material respects with applicable laws, including the Communications Act of 1934, as amended, and the communications related statutes of each state in which the Company or any of its subsidiaries operates, and the implementing rules, regulations, orders and policies of the FCC and any State PUC that regulates the business of the Company or any of its subsidiaries; and

· use commercially reasonable efforts to preserve intact our present organization, to keep available the services of our present officers and employees, to preserve our goodwill and relationships with customers, suppliers and other persons with which we have significant business dealings, to continue our current sales, marketing and other promotional policies and programs, to maintain our assets in good repair, order and condition, to maintain our insurance policies and risk management programs and, in the event of casualty or loss of any of our assets, repair or replace such assets with assets of comparable quality, and promptly notify the Parent of any material federal, state, local or foreign income or franchise and any other material suit, claim, contest, investigation, administrative or judicial proceeding or audit initiated against or with respect to the Company or any of its subsidiaries in respect of any tax matter.

We have also agreed that during the same time period, and again subject to certain exceptions or unless the Parent gives its prior written consent, we and our subsidiaries will not:

· knowingly cause or knowingly permit (to the extent that we have any control over such action being taken) any act, event or change which would reasonably be expected to have a "material adverse effect" on the Company;

· incur any indebtedness or assume, guarantee or otherwise become responsible for the obligations of any person, in either case, other than the capital lease obligations permitted under the capital expenditures limitation described below;

· amend or otherwise change our organizational documents;

· declare, set aside or pay a dividend or other distribution with respect to any of our or our subsidiaries' capital stock;

· split, combine, reclassify, or repurchase, redeem or otherwise acquire any of our or our subsidiaries' securities or any securities convertible into our or our subsidiaries' securities;

· issue or sell, or enter into any contract for the issuance or sale of, any of our or our subsidiaries' capital stock or any securities convertible into our or our subsidiaries' capital stock;

· cause to become effective our 2006 Employee Stock Purchase Plan;

· sell, assign, pledge, encumber, transfer or otherwise dispose of any of our or our subsidiaries' registered intellectual property or any other material assets;

· acquire (including by merger, consolidation, or acquisition of stock or assets) any interest in any person or any assets other than acquisitions of inventory, equipment and supplies in the ordinary course of business;

· incur any capital expenditures or commitments or additions to our or our subsidiaries' property, plant and equipment, except for capital expenditures, capital lease obligation or commitments or additions of not less than $1,500,000 in the aggregate per calendar month, as and to the extent mutually agreed by the Parent and the Company, and for certain other and additional expenditures;

- except for the taking of certain permitted actions, increase the compensation of our or any of our subsidiaries' directors, employees, consultants (including any increase pursuant to any written bonus, pension, profit-sharing or other benefit or compensation plan, policy or arrangement or commitment), or increase any such compensation or bonus payable to any of our or our subsidiaries' officers, stockholders, directors, consultants or agents having an annual salary or remuneration in excess of $100,000;

- take any action reasonably within our control to materially increase or decrease the total number of our or our subsidiaries' employees in any functioning department;

- except for the making of up to $4.3 million in severance payments as of the closing date and the payment of up to $2.5 million in bonuses, and the taking of certain other actions permitted or excepted, pay or commit to pay any retention, transaction bonus, severance or termination pay other than as required by our existing plans or agreements, or enter into any employment, deferred compensation, consulting or other similar agreement with any past or current directors, officers, employees or consultant of the Company; or adopt any additional employee benefit plan; or make any contribution to or amend or terminate or extend any pension or profit-sharing plan or other employee benefit plan; or loan or advance any money or other property to any past or current directors, officers, employees of the Company; or allow for the commencement of any new offering periods under the Company's employee stock purchase plan;

- change our independent public accountants or change our accounting methods or accounting practices;

- make or change any material tax election, incur any material tax liability or file any amended tax return, enter into any closing agreement, settlement, or compromise with respect to any tax claim or assessment related to the Company or any of its subsidiaries, knowingly surrender any right to claim a refund of taxes, or consent to any extension or waiver of the limitation period applicable to any tax claim or assessment relating to the Company or any of its subsidiaries;

- enter into, amend, modify or consent to the termination of, or fail to perform any material obligations under, any material contract or any material rights with respect to such material contract;

- pay, discharge or settle any material claim, action, proceeding or investigation litigation for an amount in excess of $100,000 individually or $250,000 in the aggregate, except to the extent reserved against in the most recent consolidated financial statements included in the SEC reports filed by the Company prior to the execution of the merger agreement;

- settle, compromise or cancel any material debts owed to or claims by us except in the ordinary course consistent with past practice or consent to the issuance of any injunction, decree, order or judgment restricting or otherwise affecting our business or operations;

- enter into any new line of business;

- take any action that would create a requirement to make a filing, registration or application with, or seek the waiver, consent or approval of, the FCC, any State PUC or municipal franchising authority or any other government entity, or discontinue or withdraw any authorized service or voluntarily relinquish any of our permits or communications licenses; or

- knowingly take or agree in writing or otherwise take any of the foregoing actions or any other action that would reasonably be expected to delay or prevent the satisfaction of any of the conditions precedent to closing the merger.

**No Solicitation of Transactions**

The merger agreement provides that we will cease any negotiations that are intended, or which could reasonably be expected, to lead to a takeover proposal and that neither we, nor our affiliates, nor our representatives (including our executive officers, directors, financial advisors, accountants, attorneys, consultants and other representatives) will:

·

directly or indirectly solicit, initiate, knowingly encourage or take any other action to knowingly facilitate a takeover proposal;

- enter into any agreement, arrangement or understanding with respect to any takeover proposal;
- initiate or participate in discussions relating to a takeover proposal;
- furnish or disclose any information to a third party with respect to a takeover proposal; or
- grant any waiver or release under any standstill agreement relating to our equity securities.

We must promptly inform the Parent of any request for information relating to a takeover proposal, any takeover proposal or any inquiry with respect to any takeover proposal, provide the Parent with any written materials received by us in connection with such request, takeover proposal or inquiry and keep the Parent fully and promptly informed as to the details of any information requested or provided and as to the details of any discussions or negotiations with respect to such request, takeover proposal or inquiry.

For purposes of the merger agreement, a "takeover proposal" means any proposal, offer or indication of interest relating to any:

- acquisition, directly or indirectly, of a business constituting 15% or more of our net revenues, net income or assets;
- acquisition, directly or indirectly, of 15% or more of the voting power of the Company;
- tender offer or exchange offer that, if consummated, would result in a third party beneficially owning 15% or more of the voting power of the Company; or
- merger, consolidation, business combination, recapitalization, liquidation, dissolution or similar transaction involving us.

Notwithstanding the foregoing, if, prior to the adoption of the merger agreement by our stockholders, but after the execution of the merger agreement, we receive an unsolicited bona fide takeover proposal that our board of directors determines in good faith (after consultation with outside counsel and a financial advisor of nationally recognized reputation) constitutes, or would be reasonably expected to lead to, a superior proposal, we may, if our board of directors determines in good faith (after consulting with outside counsel and a financial advisor of nationally recognized reputation) that it is so required in order to comply with its fiduciary duties to our stockholders under applicable law:

- furnish information regarding the Company and its subsidiaries to the person who has made the takeover proposal (provided that such person enters into a confidentiality agreement that is no less restrictive than our confidentiality agreement with the Parent), provided all such information is (or has already been) provided to the Parent; and
- participate in discussions or negotiations regarding the takeover proposal.

For purposes of the merger agreement, "superior proposal" means a bona fide written takeover proposal (with the threshold used in the definition of "takeover proposal" increased to 50% rather than 15%) on terms our board of directors determines in good faith (after consultation with our financial advisors and taking into account all of the terms and conditions of the takeover proposal and the merger agreement deemed relevant by our board, including any termination fees, conditions to expected timing and risks of consummation and the ability of the party making the takeover proposal to obtain financing, and taking into account all legal, financial, regulatory and other aspects of the takeover proposal) to be more favorable to our stockholders than the merger from a financial point of view.

We have also agreed that our board of directors will not and will not propose to:

- withhold, withdraw or modify its approval or recommendation of the merger agreement or the merger;
- recommend or approve any takeover proposal; or

· approve or recommend or allow entering into any letter of intent, memorandum of understanding, acquisition agreement or similar agreement with respect to any takeover proposal.

**Employee Benefits**

The Parent has agreed to:

· provide health benefits to any of our employees that are offered and accept continued employment by the surviving corporation, the Parent or its subsidiaries under an arrangement substantially similar to that provided to similarly-situated employees of the Parent or its subsidiaries;

· provide our employees that are offered and accept employment with the Parent and its subsidiaries, and their eligible dependents, with credit for all purposes (including for purposes of eligibility to participate, vesting, benefit accrual and eligibility to receive benefits) under any employee benefit plan, program or arrangement of the Parent, the surviving corporation or their respective subsidiaries for service accrued or deemed accrued prior to the effective time of the merger with the Company or its subsidiaries to the extent that such service was credited under the analogous plan of the Company and its subsidiaries, except that such service shall not operate to duplicate any benefit or the funding of any such benefit, and such service shall not be required to be counted with respect to any equity incentive award or benefit accrual under any defined benefit plan;

· for purposes of participation in any medical plan of the Parent (i) waive any preexisting condition limitations to the extent waived under the applicable medical plan of the Company and (ii) credit employees for any out of pocket expenditures, deductibles and employee contributions that were credited under our medical plans;

· cause the surviving corporation to honor, in accordance with their terms, all contracts and commitments as in effect immediately prior to the execution date of the merger between the us and any current or former employees or directors; and

· following the effective time of the merger, cause the surviving corporation and its subsidiaries to offer to pay, subject to receipt of a general release in customary form, severance benefits of two weeks base salary and health insurance benefits plus two weeks of base salary and such health insurance benefit for each full or partial year (in excess of the first full year) of employment with us to (i) management employees of the surviving corporation and its subsidiaries whose employment is terminated without cause within 90 days after the closing date and (ii) employees who left within 90 days after the closing date whose continued employment is conditioned upon their accepting a reduced base salary, or their principal place of employment being moved more than 50 miles away from the place they work as of the date of the execution of the merger agreement. However, an employee who is entitled to notice of termination under the WARN Act and who is terminated prior to the expiration of such notice period is only entitled to receive the excess amount of the severance described above over the amount payable to such employee under the WARN act.

**Agreement to Use Reasonable Best Efforts; Further Assurances**

Subject to the terms and conditions of the merger agreement, each party has agreed to use its reasonable best efforts to take all actions and to do all lawful things necessary, proper or advisable to consummate and make effective the transactions contemplated by the merger agreement as soon as practicable after the execution of the merger agreement and to ensure all the conditions in the merger agreement are satisfied. In furtherance of the above, each party has also agreed to use its reasonable best efforts to make appropriate applications or filings for the purpose of obtaining consents and approvals for the merger from the appropriate governmental authorities within ten (10) days after the execution of the merger agreement (or 15 days in the case of HSR filings). The Parent, however, is under no obligation whatsoever to take any action requested by any governmental authority in order to consummate the merger or other transactions contemplated by the merger agreement, including, without limitation, making any divestiture of any asset or agreeing to any type of behavioral relief that a governmental authority may request that would require the Parent to forgo revenue by providing free or reduced rate services or otherwise of more than $10,000,000 over any three years period, or to expend any amount that exceeds $10,000,000 when combined with any such foregone revenue.

Between the date of the merger agreement and the closing date, the Company and its subsidiaries agreed to maintain the validity of the communications licenses and comply in all material respects with all requirements of the communications licenses and to use reasonable best efforts to:

- refrain from taking any action that may jeopardize the validity of any of their communications licenses or result in the revocation, surrender or any adverse modification of, forfeiture of, or failure to renew under regular terms any of such licenses;
- prosecute with due diligence any pending applications with respect to their communications licenses, including any renewals of such licenses; and
- with respect to communications licenses, make all filings and reports and pay all fees necessary or reasonably appropriate for the continued operation of the businesses of the Company and its subsidiaries, as and when such approvals, consents, permits, licenses, filings, or reports or other authorizations are necessary or appropriate.

The parties have agreed to cooperate with each other to take all actions necessary to delist our common stock from the Nasdaq and to deregister our common stock under the Securities and Exchange Act of 1934 after the effective time. The parties have also agreed to take or cause to be taken all necessary action as may be reasonably requested by the other party to complete or perfect the transactions contemplated by the merger agreement.

Finally, the Company has agreed that it will reasonably cooperate with the Parent, to the extent the Parent may reasonably request, in connection with any third party financing, that Parent and Merger Sub may seek to obtain in order to fund the transactions contemplated by the merger agreement, including without limitation:

- reasonably cooperate in the preparation of any offering memorandum, private placement memorandum, prospectuses or similar documents;
- make senior management of the Company reasonably available for meetings and due diligence sessions;
- reasonably cooperate with prospective lenders, placement agents, initial purchasers and their respective advisors in performing their due diligence;
- enter into customary agreements with underwriters, initial purchasers or placement agents where expressly authorized and requested by the Parent in writing, except that no such agreement shall have any effect or be binding on the Company until the effective time of the merger; and
- enter into or help procure pledge and security documents, landlord waivers, other definitive financing documents or other requested certificates or documents where expressly authorized and requested by the Parent in writing except that no such agreement shall have any effect or be binding on the Company until the effective time of the merger;
- notwithstanding the foregoing, nothing in the merger agreement requires the Company and its subsidiaries to pay any commitment or similar fee or incur any other liability in connection with any third party financing prior to the effective time and the Parent has agreed to, at our request, reimburse us for all reasonable out-of-pocket costs incurred by us in connection with such cooperation. In addition, no claims by the Parent may arise out of any compliance or non-compliance by the Company or its subsidiaries with the foregoing obligations and such compliance or non-compliance may not be a defense or mitigating factor to any claim by the Company for breach of the merger agreement.

**Conditions to the Merger**

The obligations of the parties to complete the merger are subject to the following mutual conditions:

- receipt of Company stockholder approval;
- the absence of any governmental order, decree, judgment, injunction or other ruling which prevents or prohibits the consummation of the merger;

· the expiration or termination of the waiting period under the Hart-Scott-Rodino Act;

· the receipt of applicable consents and approvals from the FCC; and

· the receipt of applicable consents and approvals from State PUCs that regulate the Company's business or the business of any of its subsidiaries.

The obligations of the Parent and the Merger Sub to complete the merger are subject to the following additional conditions:

· the truth and correctness of our representations and warranties as of the date of the merger agreement and, except where the failure of our representations and warranties to be true and correct would not reasonably be expected to have a material adverse effect on us and our subsidiaries, individually or in the aggregate, the truth and correctness of our representations and warranties (without giving effect for any materiality or material difference qualification therein) as of the closing date or as of the earlier date for such representations and warranties as expressly relate to an earlier date, and the truth and correctness of our representations and warranties with respect to authority and approvals, absence of material adverse change and brokers as of the closing date as if made on and as of the closing date;

· the absence of any pending proceedings, order, decree, judgment, injunction or other ruling prohibiting the consummation of the merger;

· the receipt of the final order of each of the applicable consents, approvals, orders and authorizations;

· the performance and compliance, in all material respects, by us of our agreements and conditions in the merger agreement;

· our delivery to the Parent at closing of a certificate with respect to our representations, warranties, agreements and conditions;

· since September 22, 2006, the date of execution of the merger agreement, no "material adverse effect" with respect to the Company shall have occurred and be continuing;

· we meet a defined minimum financial performance measure based on our operating income for the quarter ended September 30, 2006 as adjusted for a number of items;

· the resignation of our directors;

· our certification that we are not, and have not been during the past five years, a United States real property holding company; and

· the release of certain liens and the termination of all financial statements related to such liens.

For the purposes of the merger agreement, a "material adverse effect" with respect to the Company means any event, change or effect that has had, or would reasonably be expected to have a material adverse effect on (i) the business, operation, financial condition, assets, liabilities or results of operations of the Company and its subsidiaries, taken as a whole, or (ii) the ability of the Company to perform its obligations under the merger agreement or consummate the transactions contemplated by the merger agreement. A "material adverse effect" with respect to the Company does not include such effect arising out of or resulting from the following:

· changes in unbundled network element availability and rates consistent and in accordance with the rules, regulations and laws established and implemented by the FCC and the applicable State PUCs;

· changes or effects which are or result from occurrences relating to the United States economy or securities or financial markets generally or the industries in which the Company operates that in either case do not disproportionately affect the Company and its subsidiaries;

- changes or effects which result from the announcement of the merger agreement, the merger or the transactions contemplated by the merger agreement;

- changes or effects which are or result from changes in applicable laws after the execution of the merger agreement but only if such changes do not disproportionately affect the Company and its subsidiaries relative to similarly situated companies;

- changes or effects which are or result from changes in GAAP after the execution of the merger agreement; or

- changes or effects which are or result from actions taken by the Parent with respect to the merger or the Company and its subsidiary, including the Parent's unreasonably withholding its consent to the Company's taking certain action otherwise prohibited.

Our obligation to complete the merger is subject to the following additional conditions:

- the truth and correctness of the Parent's and the Merger Sub's representations and warranties (without regard to materiality qualifications), except where the failure of the Parent's and the Merger Sub's representations and warranties to be true and correct would not, individually or in the aggregate, reasonably be expected to have a material adverse effect on the ability of the Parent and the Merger Sub to perform their obligations under the merger agreement;

- the performance, in all material respects, by the Parent and the Merger Sub of their agreements and conditions in the merger agreement; and

- the delivery at closing by the Parent of a certificate with respect to the Parent's and the Merger Sub's representations, warranties, agreements and conditions.

**Termination**

The merger agreement may be terminated and the merger may be abandoned at any time prior to the effective time of the merger, whether before or after stockholder approval has been obtained, as follows:

- by mutual written consent of the parties;

- by either the Parent or the Company if:

- our stockholders fail to adopt the merger agreement at the Special Meeting or any adjournment of the Special Meeting;

- the closing has not occurred on or before January 31, 2007, so long as the failure to complete the merger is not the result of the failure of the terminating party to comply with the terms of the merger agreement;

- there is any law or final, non-appealable government order, decree or ruling that prevents completion of the merger, so long as such law, government order, decree or ruling is not the result of the failure of the terminating party to fulfill its obligations under the merger agreement; or

- there is a breach by the non-terminating party of its representations, warranties, agreements or covenants in the merger agreement such that the closing conditions would not be satisfied, which breach has not been cured within 20 business days (or is incapable of being cured before the termination date);

· by us if:

· prior to adoption of the merger agreement by our stockholders (i) our board of directors has received a superior proposal, (ii) our board determines in good faith (after consultation with outside counsel and a financial advisor of nationally recognized reputation) that taking such action is required for the members of our board of directors to comply with their fiduciary duties to our stockholders under applicable law, (iii) we have complied with our non-solicitation covenant and have prepared this proxy solicitation and called a meeting of our stockholders, (iv) we provide the Parent written notice that our board of directors intends to take such action, (v) we negotiate in good faith with the Parent for three business days to modify the terms and conditions of the merger agreement such that the revised terms and conditions would enable us to proceed with the consummation of the merger and (vi) we pay the termination fee described below under “The Merger Agreement — Termination Fees and Expenses”;

· by Parent if:

· our board withdraws or modifies in a manner adverse to the Parent its recommendation that the Company's stockholders adopt the merger agreement or recommends, approves or adopts a takeover proposal;

· we fail to include in this proxy statement the recommendation of our board that you vote in favor of the merger;

· our board fails to publicly reaffirm its recommendation within 10 days of being requested by the Parent to do so;

· a third party commences a tender or exchange offer for the Company and our board does not recommend rejection of the offer within 10 days;

· a takeover proposal is publicly announced and we fail to issue within 10 days of such announcement a press release reaffirming the board's recommendation of the merger agreement; or

· we fail to call and hold the Special Meeting and timely mail this proxy statement, which is not cured within 10 business days following receipt by the Company of a notice of such breach.

**Termination Fees and Expenses**

We have agreed to pay to the Parent a termination fee of $6.25 million if:

· either the Company or the Parent has terminated the merger agreement because of the failure to receive Company stockholder approval; and

· prior to termination of the merger agreement, a takeover proposal has been publicly announced or otherwise communicated to our board of directors; and

· within 12 months after the termination, the Company enters into or completes a takeover proposal;

· either the Company or the Parent has terminated the merger agreement because the merger has not been completed by January 31, 2007; and

· prior to termination of the merger agreement, a takeover proposal has been publicly announced or otherwise communicated to our board of directors; and

· within 12 months after the termination, the Company enters into or completes a takeover proposal;

· the Parent has terminated the merger agreement due to a breach by us of our representations, warranties, agreements or conditions such that the closing conditions would not be satisfied, which breach has not been cured within 20 business days; and

· prior to termination of the merger agreement, a takeover proposal has been publicly announced or otherwise communicated to our board of directors; and

· within 12 months after the termination, we enter into or complete a takeover proposal;

· the Company has terminated the merger agreement, prior to the Special Meeting, if we receive a superior proposal in accordance with the terms of the merger agreement, but only after we have provided notice to the Parent regarding the superior proposal and provided the Parent with a three business day period, during which time we negotiated in good faith with the Parent, to make an offer that is at least as favorable as the superior proposal; or

· the Parent has terminated the merger agreement because (i) our board withdraws or modifies in a manner adverse to the Parent its recommendation that the Company's stockholders adopt the merger agreement or recommends, approves or adopts a takeover proposal, (ii) we fail to include in this proxy statement (or any amendment) the recommendation of our board that you vote in favor of the merger, (iii) our board fails to publicly reaffirm its recommendation within 10 days of being requested by the Parent to do so, (iv) a third party commences a tender or exchange offer for the Company and our board does not recommend rejection of the offer within 10 days, (v) a takeover proposal is publicly announced and we fail to issue within 10 days of such announcement a press release reaffirming the board's recommendation of the merger agreement, or (vi) we fail to call and hold the Special Meeting and timely mail this proxy statement, which is not cured within 10 business days following receipt by the Company of a notice of such breach.

In addition, we have agreed to reimburse the Parent's out-of-pocket transaction expenses, up to a limit of $1.25 million, if:

· either the Company or the Parent has terminated the merger agreement because of the failure to receive Company stockholder approval and, prior to termination of the merger agreement, a takeover proposal has been publicly announced or otherwise communicated to our board of directors;

· either the Company or the Parent has terminated the merger agreement because the merger has not been completed by January 31, 2007, and prior to termination of the merger agreement, a takeover proposal has been publicly announced or otherwise communicated to our board of directors;

· the Parent has terminated the merger agreement due to a breach by us of our representations, warranties, agreements or conditions such that the closing conditions would not be satisfied, which breach has not been cured within 20 business days, and prior to termination of the merger agreement, a takeover proposal has been publicly announced or otherwise communicated to our board of directors;

· the Company has terminated the merger agreement, prior to the Special Meeting, if we receive a superior proposal in accordance with the terms of the merger agreement, but only after we have provided notice to the Parent regarding the superior proposal and provided the Parent with a three business day period, during which time we negotiated in good faith with the Parent, to make an offer that is at least as favorable as the superior proposal; or

· the Parent has terminated the merger agreement because (i) our board withdraws or modifies in a manner adverse to the Parent its recommendation that the Company's stockholders adopt the merger agreement or recommends, approves or adopts a takeover proposal, (ii) we fail to include in this proxy statement (or any amendment) the recommendation of our board that you vote in favor of the merger, (iii) our board fails to publicly reaffirm its recommendation within 10 days of being requested by the Parent to do so, (iv) a third party commences a tender or exchange offer for the Company and our board does not recommend rejection of the offer within 10 days, (v) a takeover proposal is publicly announced and we fail to issue within 10 days of such announcement a press release reaffirming the board's recommendation of the merger agreement, or (vi) we fail to call and hold the Special Meeting and timely mail this proxy statement, which is not cured within 10 business days following receipt by the Company of a notice of such breach.

For purposes of determining whether transaction expenses or a termination fee is payable by us, a "takeover proposal" means any proposal, offer or indication of interest relating to any:

- acquisition, directly or indirectly, of a business constituting 35% or more of our net revenues, net income or assets;
- acquisition, directly or indirectly, of 35% or more of the voting power of the Company;
- tender offer or exchange offer that, if consummated, would result in a third party beneficially owning 35% or more of the voting power of the Company; or
- merger, consolidation, business combination, recapitalization, liquidation, dissolution or similar transaction involving us.

**Amendment and Waiver**

The merger agreement may be amended prior to the effective time of the merger by mutual consent of the parties. After approval of the merger by our stockholders, no amendment will be made except as allowed under applicable law. The merger agreement provides that, at any time prior to the effective time of the merger, any party may extend the time for the performance of any of the obligations or other acts of the other parties, waive any inaccuracies in the representations and warranties of the other parties or waive compliance with any agreement of another party or any condition to its own obligations contained in the merger agreement.

**Expenses**

Subject to the provisions relating to reimbursement of fees and expenses in the event of termination as described in "The Merger Agreement— Termination Fees and Expenses," each party will pay its own fees and expenses incurred in connection with the merger except that each of the Company and the Parent will pay one-half of the expenses incurred in connection with the filing of pre-merger notification and report forms under the Hart-Scott-Rodino Act.

## MARKET PRICES OF THE COMPANY'S STOCK

Our common stock is traded on Nasdaq under the symbol "TALK." The following table sets forth the high and low sales prices per share of our common stock for the periods indicated.

**Market Information**

| | **Common Stock** | |
|---|---|---|
| | **High** | **Low** |
| Fiscal Year Ended December 31, 2006: | | |
| 1st Quarter | **$10.20** | $8.36 |
| 2nd Quarter | $9.25 | $6.06 |
| 3rd Quarter | $9.69 | $5.47 |
| 4th Quarter (through [ ], 2006) | | |
| Fiscal Year Ended December 31, 2005: | | |
| 1st Quarter | $ 6.71 | $ 5.85 |
| 2nd Quarter | $ 10.21 | $ 6.26 |
| 3rd Quarter | $ 11.61 | $ 8.58 |
| 4th Quarter | $ 10.01 | $ 8.63 |
| Fiscal Year Ended December 31, 2004: | | |
| 1st Quarter | $ 12.05 | $ 8.14 |
| 2nd Quarter | $ 10.05 | $ 7.07 |

| | | |
|---|---|---|
| 3rd Quarter | $ 7.70 | $ 5.05 |
| 4th Quarter | $ 7.47 | $ 5.01 |

The closing sale price of our common stock on Nasdaq on September 21, 2006, which was the last trading day before we announced the merger, was $6.57. The closing sale price of our common stock on Nasdaq on September 27, 2006, which was the last trading day before Sun Capital's filing with the SEC that included a copy of their September 28 letter to our Board proposing to purchase the Company for $9.00 cash per share, was $8.32. On [ ], 2006, the last trading day before the date of this proxy statement, the closing price for the Company’s common stock on Nasdaq was $[ ]. You are encouraged to obtain current market quotations for Talk America’s common stock in connection with voting your shares.

During the two prior fiscal years, we have not paid any cash dividends on our common stock and we are currently restricted by the terms of the merger agreement from paying any dividends.

## SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth certain information known to the Company with respect to beneficial ownership of the Company common stock as of September 29, 2006 (except as otherwise noted) by (i) each stockholder who is known by the Company to own beneficially more than five percent of the outstanding common stock, (ii) each of the Company’s directors, (iii) each of the executive officers named below and (iv) all current directors and executive officers of the Company as a group. Except as otherwise indicated below, the Company believes that the beneficial owners of the common stock listed below have sole investment and voting power with respect to such shares.

| **Name of Beneficial Owner or Identity of Group** | **Number of Shares Beneficially Owned (1)** | **Percent of Shares Beneficially Owned** |
|---|---|---|
| Sun Capital<br>5200 Town Center Circle, Suite 470,<br>Boca Raton, Florida 33486 | 4,242,520 (2) | 13.9% |
| Eton Park Fund, L.P., Eton Park Master Fund, Ltd., Eton Park Associates, L.P., Eton Park Capital Management, L.P., Eric M. Mindich<br>825 Third Avenue, 8th Floor<br>New York, NY 10022 | 2,800,000(3) | 9.2% |
| Jonathan Starr, Flagg Street Capital LLC, Flagg Street Partners LP, Flagg Street Partners Qualified LP and Flagg Street Offshore LP.<br>44 Brattle Street<br>Cambridge, MA 02138 | 2,777,882(4) | 9.2% |
| North Run Capital<br>One International Place, Suite 2401<br>Boston, MA 02110 | 2,438,500 (5) | 8.0% |
| Barclays Global Investors, NA., Barclays Global Fund Advisors, Barclays Global Investors, Ltd., Barclays Global Investors | 2,406,912(6) | 7.9% |

| | | |
|---|---|---|
| Japan Trust and Banking Company Limited<br>45 Fremont Street<br>San Francisco, CA 94105 | | |
| Paul Rosenberg<br>650 N. E. 5th Avenue<br>Boca Raton, FL 33432 | 1,919,995(7) | 6.3% |
| Mellon Financial Corporation<br>One Mellon Center<br>Pittsburgh, PA 15258 | 1,751,170(8) | 5.8% |
| Dimensional Fund Advisors Inc.<br>1299 Ocean Avenue, 11th Floor<br>Santa Monica, CA 90401 | 1,684,002(9) | 5.5% |
| Gabriel Battista | 646,666(10) | 2.1% |
| Mark S. Fowler | 137,374(10) | * |
| Edward B. Meyercord, III | 556,667(10) | 1.8% |
| Ronald R. Thoma | 59,311(10) | * |
| Robert Korzeniewski | 21,000(10) | * |
| Aloysius T. Lawn, IV | 232,499(10) | * |
| Jeffrey Earhart | 145,768(10) | * |
| Warren Brasselle | 148,166(10) | * |
| Patrick O'Leary | 75,000(10) | * |
| All directors and executive officers as a group (14 persons) | 2,467,117(10) | 7.5% |

* Less than 1%

(1) The securities "beneficially owned" by a person are determined in accordance with the definition of "beneficial ownership" set forth in the regulations of the SEC and, accordingly, may include securities owned by or for, among others, the spouse, children or certain other relatives of such person. The same shares may be beneficially owned by more than one person. Beneficial ownership may be disclaimed as to certain of the securities.

(2) The foregoing information is derived from the Schedule 13D filed by SCSF Equities, LLC, Sun Capital Securities Offshore Fund, Ltd., Sun Capital Securities Fund, LP, Sun Capital Securities Advisors, LP, Sun Capital Securities, LLC, Marc J. Leder and Rodger R. Krouse on September 28, 2006.

(3) The foregoing information is derived from the Schedule 13G/A filed by Eton Park Fund, L.P., Eton Park Master Fund, Ltd., Eton Park Associates, L.P., Eton Park Capital Management, L.P. and Eric M. Mindich on February 8, 2006. This Schedule indicates that, as of December 31, 2005: Eton Park Fund, L.P. had beneficial ownership of 980,000 shares, with shared voting power and shared dispositive power for 980,000 shares; Eton Park Master Fund Ltd. had beneficial ownership of 1,820,000 shares, with shared voting power and shared dispositive power over 1,820,000 shares; Eton Park Associates, L.P. had beneficial ownership of 980,000 shares, with shared voting power and shared dispositive power for 980,000 shares; Eton Park Capital Management, L.P. had beneficial ownership of 1,820,000 shares, with shared voting power and shared dispositive power for 1,820,000 shares, and; Eric M. Mindich had beneficial ownership of 2,800,000 shares, with shared voting power and shared dispositive power for 2,800,000 shares.

(4) The foregoing information is derived from the Schedule 13D/A filed by Flagg Street Capital LLC, Flagg Street Partners LP, Flagg Street Partners Qualified LP, Flagg Street Offshore, LP and Jonathan Starr on September 27, 2006. This Schedule indicates that, as of September 27, 2006: Jonathan Starr, had beneficial ownership of 2,777,882 shares, with sole voting power for 2,777,882 shares and sole dispositive power for 2,777,882 shares; Flagg Street Capital LLC had beneficial ownership of 2,777,882 shares, with sole voting power for 2,777,882 shares and sole dispositive power for 2,777,882 shares; Flagg Street Partners LP had beneficial ownership of 328,760 shares, with sole voting power for 328,760 shares and sole dispositive power for 328,760 shares, Flagg Street Partners Qualified LP had beneficial ownership of 649,353 shares, with sole voting power for 649,353 shares and sole dispositive power for 649,353 shares, and Flagg Street Offshore LP had beneficial ownership of 1,799,769 shares, with sole voting power for 1,799,769 shares and sole dispositive power for 1,799,769 shares.

(5) The foregoing information is derived from the Schedule 13G filed by North Run Capital, LP, North Run GP, LP, North Run Advisors, LLC, Todd B. Hammer and Thomas B. Ellis on July 21, 2006.

(6) The foregoing information is derived from the Schedule 13G filed by Barclays Global Investors, NA, Barclays Global Fund Advisors, Barclays Global Investors, Ltd. and Barclays Global Investors Japan Trust and Banking Company Limited on January 26, 2006. This Schedule indicates that, as of December 31, 2005: Barclays Global Investors, NA had beneficial ownership of 2,406,912 shares, with sole voting power for 2,141,523 shares and sole dispositive power for 2,406,912 shares; Barclays Global Fund Advisors had beneficial ownership of 341,217 shares, with sole voting power and sole dispositive power for 341,217 shares; and Barclays Global Investors, Ltd. and Barclays Global Investors Japan Trust and Banking Company Limited had no beneficial ownership.

(7) The foregoing information is derived from the Schedule 13D/A filed by Paul Rosenberg, the Rosenberg Family Limited Partnership, PBR, Inc. and the New Millennium Charitable Foundation on February 12, 1999.

(8) The foregoing information is derived from the Schedule 13G filed by Mellon Financial Corporation on February 15, 2006. This Schedule indicates that, as of December 31, 2005, Mellon Financial Corporation had beneficial ownership of 1,751,170 shares, with sole voting power for 955,137 shares and sole dispositive power for 1,706,670 shares.

(9) The foregoing information is derived from the Schedule 13G filed by Dimensional Fund Advisors Inc. on February 6, 2006.

(10) Includes shares of our common stock that could be acquired upon exercise of options exercisable within 60 days after September 29, 2006 (without giving effect to any vesting by reason of the consummation of the merger) as follows: Gabriel Battista - 626,665; Mark S. Fowler - 50,000; Edward B. Meyercord, III - 550,000; Ronald R. Thoma - 40,000; Robert Korzeniewski - 20,000; Aloysius T. Lawn, IV - 232,499; Jeffrey Earhart - 141,000; Warren Brasselle - 138,333; Patrick O'Leary - 75,000; and all directors and executive officers as a group - 2,300,164.

## DISSENTERS' RIGHTS OF APPRAISAL

Under the DGCL, you have the right to dissent from the merger and to receive payment in cash for the fair value of your common stock of the Company, exclusive of any element of value arising from the accomplishment or expectation of the merger, together with a fair rate of interest, as determined by the Delaware Court of Chancery. The Company's stockholders electing to exercise appraisal rights must comply with the provisions of Section 262 of the DGCL in order to perfect their rights. The Company will require strict compliance with the statutory procedures.

The following is intended as a brief summary of the material provisions of the Delaware statutory procedures required to be followed by a stockholder in order to dissent from the merger and perfect appraisal rights. This summary, however, is not a complete statement of all applicable requirements and is qualified in its entirety by reference to Section 262 of the DGCL, the full text of which appears in Annex C to this proxy statement. This summary does not constitute legal advice, nor does it constitute a recommendation that Company stockholders exercise their appraisal rights under Section 262.

Section 262 requires that, where a merger agreement is to be submitted for adoption at a stockholders' meeting, stockholders be notified that appraisal rights will be available not less than 20 days before the Special Meeting to vote on the merger. A copy of Section 262 must be included with such notice. This proxy statement constitutes the Company's notice to its stockholders of the availability of appraisal rights in connection with the merger in compliance with the requirements of Section 262. If you wish to consider exercising your appraisal rights, you should carefully review the text of Section 262 contained in Annex C since failure to timely and properly comply with the requirements of Section 262 will result in the loss of your appraisal rights under Delaware law.

If you elect to demand appraisal of your shares, you must satisfy each of the following conditions:

- You must deliver to the Company a written demand for appraisal of your shares before the vote with respect to the merger is taken. This written demand for appraisal must be in addition to and separate from any proxy or vote abstaining from or voting against the adoption of the merger agreement. A holder of shares of common stock of the Company wishing to exercise appraisal rights must hold the shares of record on the date that the written demand for appraisal is made and must continue to hold the shares of record through the effective date of the merger, since appraisal rights will be lost if the shares are transferred prior to the effective date of the merger. Voting against or failing to vote for the adoption of the merger agreement by itself does not constitute a demand for appraisal within the meaning of Section 262.

- You must not vote in favor of the adoption of the merger agreement. A vote in favor of the adoption of the merger agreement, by proxy or in person, will constitute a waiver of your appraisal rights in respect of the shares so voted and will nullify any previously filed written demands for appraisal. A proxy that is signed and does not contain voting instructions will, unless revoked, be voted in favor of the adoption of the merger agreement, and it will constitute a waiver of the stockholder's right of appraisal and will nullify any previously delivered written demand for appraisal. Therefore, a stockholder who votes by proxy and who wishes to exercise appraisal rights must vote against the adoption of the merger agreement or abstain from voting on the merger agreement.

If you fail to comply with either of these conditions and the merger is completed, you will be entitled to receive the cash payment for your shares of the Company's common stock as provided for in the merger agreement, but you will have no appraisal rights with respect to your shares of the Company's common stock.

All demands for appraisal should be addressed to Talk America Holdings, Inc., 6805 Route 202, New Hope, Pennsylvania, Attention: Aloysius T. Lawn IV, Executive Vice President -- General Counsel and Secretary, telephone: (215) 862-1500, before the vote on the merger agreement is taken at the Special Meeting, and should be executed by, or on behalf of, the record holder of the shares of the Company's common stock. The demand must reasonably inform the Company of the identity of the stockholder and the intention of the stockholder to demand appraisal of his, her or its shares.

To be effective, a demand for appraisal by a holder of the Company's common stock must be made by, or in the name of, such registered stockholder, fully and correctly, as the stockholder's name appears on his or her stock certificate(s). Beneficial owners who do not also hold the shares of record may not directly make appraisal demands to the Company. The beneficial holder must, in such cases, have the registered owner submit the required demand in respect of those shares. If shares are held of record in a fiduciary capacity, such as by a trustee, guardian or custodian, execution of a demand for appraisal should be made in that capacity; and if the shares are held of record by more than one person, as in a joint tenancy or tenancy in common, the demand should be executed by or for all joint owners. An authorized agent, including an authorized agent for two or more joint owners, may execute the demand for appraisal for a stockholder of record; however, the agent must identify the record holder or holders and expressly disclose the fact that, in executing the demand, he or she is acting as agent for the record holder. A record holder, such as a broker, who holds shares as a nominee for others, may exercise his or her right of appraisal with respect to the shares held for one or more beneficial owners, while not exercising this right for other beneficial owners. In that case, the written demand should state the number of shares as to which appraisal is sought. Where no number of shares is expressly mentioned, the demand will be presumed to cover all shares held in the name of the record holder.

If you hold your shares of the Company's common stock in a brokerage account or in other nominee form and you wish to exercise appraisal rights, you should consult with your broker or the other nominee to determine the appropriate procedures for the making of a demand for appraisal by the nominee.

Within 10 days after the effective time of the merger, the surviving corporation must give written notice that the merger has become effective to each Company stockholder who has properly filed a written demand for appraisal and who did not vote in favor of the merger agreement. At any time within 60 days after the effective time, any stockholder who has demanded an appraisal has the right to withdraw the demand and to accept the cash payment specified by the merger agreement for his or her shares of the Company's common stock. Within 120 days after the effective time, either the surviving corporation or any stockholder who has complied with the requirements of Section 262 may file a petition in the Delaware Court of Chancery demanding a determination of the fair value of the shares held by all stockholders entitled to appraisal. The surviving corporation has no obligation, and no present intention, to file such a petition in the event there are dissenting stockholders. Accordingly, the failure of a stockholder to file such a petition within the period specified could nullify the stockholder's previously written demand for appraisal.

Within 120 days after the effective time of the merger, any stockholder who has complied with Section 262 will be entitled, upon written request, to receive a statement setting forth the aggregate number of shares of Company common stock with respect to which demands for appraisal have been received and the aggregate number of holders of such shares. The statement must be mailed within ten days after a written request therefor has been received by the surviving corporation or within ten days after the expiration of the period for delivery of demands for appraisal, whichever is later.

If a petition for appraisal is duly filed by a stockholder and a copy of the petition is delivered to the surviving corporation, the surviving corporation will then be obligated, within 20 days after receiving service of a copy of the petition, to provide the Chancery Court with a duly verified list containing the names and addresses of all stockholders who have demanded an appraisal of their shares. After notice to stockholders who have demanded an appraisal of their shares, the Chancery Court is empowered to conduct a hearing upon the petition, and to determine those stockholders who have complied with Section 262 and who have become entitled to the appraisal rights provided thereby. The Chancery Court may require the stockholders who have demanded payment for their shares to submit their stock certificates to the Register in Chancery for notation thereon of the pendency of the appraisal proceedings; and if any stockholder fails to comply with that direction, the Chancery Court may dismiss the proceedings as to that stockholder.

After determination of the stockholders entitled to appraisal of their shares of the Company's common stock, the Chancery Court will appraise the shares, determining their fair value exclusive of any element of value arising from the accomplishment or expectation of the merger, together with a fair rate of interest. When the value is determined, the Chancery Court will direct the payment of such value, with interest thereon accrued during the pendency of the proceeding, if the Chancery Court so determines, to the stockholders entitled to receive the same, upon surrender by such holders of the certificates representing those shares.

In determining fair value and, if applicable, a fair rate of interest, the Chancery Court is required to take into account all relevant factors. In Weinberger v. UOP, Inc., the Supreme Court of Delaware discussed the factors that could be considered in determining fair value in an appraisal proceeding, stating that "proof of value by any techniques or methods that are generally considered acceptable in the financial community and otherwise admissible in court" should be considered, and that "fair price obviously requires consideration of all relevant factors involving the value of a company." The Delaware Supreme Court stated that, in making this determination of fair value, the court must consider market value, asset value, dividends, earnings prospects, the nature of the enterprise and any other facts that could be ascertained as of the date of the merger that throw any light on future prospects of the merged corporation. Section 262 provides that fair value is to be "exclusive of any element of value arising from the accomplishment or expectation of the merger." In Cede & Co. v. Technicolor, Inc., the Delaware Supreme Court stated that such exclusion is a "narrow exclusion [that] does not encompass known elements of value," but which rather applies only to the speculative elements of value arising from such accomplishment or expectation. In Weinberger, the Supreme Court of Delaware also stated that "elements of future value, including the nature of the enterprise, which are known or susceptible of proof as of the date of the merger and not the product of speculation, may be considered." You should be aware that the fair value of your shares as determined under Section 262 could be more, the same, or less than the value that you are entitled to receive under the terms of the merger agreement.

Costs of the appraisal proceeding may be imposed upon the surviving corporation and the stockholders participating in the appraisal proceeding by the Chancery Court as the Chancery Court deems equitable in the circumstances. Upon the application of a stockholder, the Chancery Court may order all or a portion of the expenses incurred by any stockholder in connection with the appraisal proceeding, including, without limitation, reasonable attorneys' fees and the fees and expenses of experts, to be charged pro rata against the value of all shares entitled to appraisal. Any stockholder who had demanded appraisal rights will not, after the effective time, be entitled to vote shares subject to that demand for any purpose or to receive payments of dividends or any other distribution with respect to those shares, other than with respect to payment as of a record date prior to the effective time; however, if no petition for appraisal is filed within 120 days after the effective time of the merger, or if the stockholder delivers a written withdrawal of his or her demand for appraisal and an acceptance of the terms of the merger within 60 days after the effective time of the merger, then the right of that stockholder to appraisal will cease and that stockholder will be entitled to receive the cash payment for shares of his, her or its Company common stock pursuant to the merger agreement. Any withdrawal of a demand for appraisal made more than 60 days after the effective time of the merger may only be made with the written approval of the surviving corporation and must, to be effective, be made within 120 days after the effective time.

In view of the complexity of Section 262, the Company's stockholders who may wish to dissent from the merger and pursue appraisal rights should consult their legal advisors.

## WHERE YOU CAN FIND ADDITIONAL INFORMATION

The Company files annual, quarterly and current reports, proxy statements and other information with the SEC. You may read and copy any reports, proxy statements or other information that we file with the SEC at the following location of the SEC:

Public Reference Room
100 F Street, N.E.
Washington, D.C. 20549

Please call the SEC at 1-800-SEC-0330 for further information on the public reference rooms. You may also obtain copies of this information by mail from the Public Reference Section of the SEC, 100 F Street, N.E., Washington, D.C. 20549, at prescribed rates. The Company's public filings are also available to the public from document retrieval services and the Internet website maintained by the SEC at www.sec.gov.

Any person, including any beneficial owner, to whom this proxy statement is delivered may request copies of reports, proxy statements or other information concerning us, without charge, by written or telephonic request directed to us at Talk America Holdings, Inc., 6805 Route 202, New Hope, Pennsylvania, Attention: Aloysius T. Lawn IV, Executive Vice President, Secretary and General Counsel, telephone: (215) 862-1500. If you would like to request documents, please do so by [ ], 2006, in order to receive them before the Special Meeting.

No persons have been authorized to give any information or make any representations other than those contained in this proxy statement and, if given or made, such information or representations must not be relied upon as having been authorized by us or any other person. This proxy statement is dated [ ], 2006. You should not assume that the information contained in this proxy statement is accurate as of any date other than that date, and the mailing of this proxy statement to stockholders shall not create any implication to the contrary.

Neither the SEC nor any state securities commission has approved or disapproved the merger, passed upon the merits or fairness of the merger agreement or the transactions contemplated thereby, including the proposed merger, or passed upon the adequacy or accuracy of the information contained in this document. Any representation to the contrary is a criminal offense.

**ANNEX A**

AGREEMENT AND PLAN OF MERGER

**AGREEMENT AND PLAN OF MERGER**

**BY AND AMONG**

**TALK AMERICA HOLDINGS, INC.,**

**CAVALIER ACQUISITION CORP.**

**AND**

**CAVALIER TELEPHONE CORPORATION**

**Dated as of September 22, 2006**

TABLE OF CONTENTS

Section 4.5 Brokers.
Section 4.6 Litigation.
Section 4.7 Operations of Merger Sub.
Section 4.8 Financing Wherewithal.

**THIS AGREEMENT AND PLAN OF MERGER** (this “**Agreement**”), dated as of September 22, 2006, is by and among Cavalier Telephone Corporation, a Delaware corporation (“**Buyer**”), Cavalier Acquisition Corp., a Delaware corporation (“**Merger Sub**”) and a wholly-owned subsidiary of CavTel Holdings, LLC, a Delaware limited liability company of which Buyer is the sole member, and Talk America Holdings, Inc., a Delaware corporation (the “**Company**”).

## INTRODUCTION

A. The respective Boards of Directors of each of Buyer, Merger Sub and the Company have unanimously (i) approved, and declared advisable and in the best interests of Buyer, Merger Sub and the Company and their respective stockholders, the merger of Merger Sub with and into the Company (the “**Merger**”) in accordance with the provisions of the Delaware General Corporation Law (the “**DGCL**”), and subject to the terms and conditions of this Agreement and (ii) approved this Agreement.

B. Buyer, Merger Sub and the Company desire to make certain representations, warranties, covenants and agreements in connection with the Merger and also to prescribe various conditions to the Merger.

C. Certain capitalized terms have the meanings set forth in Section 9.1.

## AGREEMENT

In consideration of the mutual representations, warranties, covenants and other agreements set forth herein, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto agree as follows:

## ARTICLE I
## THE MERGER

Section 1.1 The Merger.

At the Effective Time, subject to the terms and conditions of this Agreement and in accordance with the DGCL, (i) Merger Sub shall be merged with and into the Company; (ii) the separate corporate existence of Merger Sub shall cease; and (iii) the Company shall be the surviving corporation (the Company, as the surviving corporation in the Merger is sometimes referred to herein as the “**Surviving Corporation**”) and shall continue its legal existence under the DGCL.

Section 1.2 Effective Time; Closing Date.

Subject to the terms and conditions of this Agreement, the Company and Merger Sub shall cause the Merger to be consummated on the Closing Date by filing a certificate of merger with the Secretary of State of the State of Delaware (the “**Certificate of Merger**”). The Merger shall become effective at such time as the Certificate of Merger is duly filed in accordance with the provisions of Section 251 of the DGCL, or at such later time as may be stated by the parties in the Certificate of Merger (the “**Effective Time**”, and the date that includes the Effective Time, the “**Effective Date**”). The closing of the Merger (the “**Closing**”) shall take place at the offices of Edwards Angell Palmer & Dodge LLP in Boston, Massachusetts, at 10:00 a.m., Boston time, two Business Days after the date on which the last of the conditions set forth in Article VI shall have been satisfied or waived (other than those conditions that by their nature are to be satisfied at the Closing, but subject to the satisfaction or waiver of those conditions), or on such other date, time and place as the Company and Buyer may mutually agree in writing (such date on which the Closing actually occurs being referred to herein as the “**Closing Date**”).

Section 1.3 Effect of the Merger.

At the Effective Time, the effect of the Merger shall be as provided in the applicable provisions of the DGCL. Without limiting the generality of the foregoing, and subject thereto, at the Effective Time, all the property, rights, privileges, powers, franchises and assets of the Company and Merger Sub shall vest in the Surviving Corporation, and all debts, liabilities, obligations and duties of the Company and Merger Sub shall become the debts, liabilities, obligations and duties of the Surviving Corporation.

Section 1.4 Certificate of Incorporation; By-laws.

(a) The certificate of incorporation of Merger Sub, as in effect immediately prior to the Effective Time, shall be the certificate of incorporation of the Surviving Corporation until thereafter amended as provided by Law and such certificate of incorporation.

(b) The by-laws of Merger Sub, as in effect immediately prior to the Effective Time, shall be the by-laws of the Surviving Corporation, until thereafter amended as provided by Law and such by-laws.

Section 1.5 Board of Directors and Officers.

The Board of Directors and the officers of Merger Sub immediately prior to the Effective Time shall, from and after the Effective Time, be the Board of Directors and officers, respectively, of the Surviving Corporation, each to hold office until his or her respective successors are duly elected or appointed and qualified or until their earlier death, resignation or removal in accordance with the certificate of incorporation and by-laws of the Surviving Corporation.

Section 1.6 Further Assurances.

If at any time after the Effective Time the Surviving Corporation shall consider or be advised that any deeds, bills of sale, assignments or assurances or any other acts or things are necessary, desirable or proper (a) to vest, perfect or confirm, of record or otherwise, in the Surviving Corporation, its right, title or interest in, to or under any of the properties, rights, privileges, powers, franchises or assets of either the Company or Merger Sub or (b) otherwise to carry out the purposes of this Agreement, the Surviving Corporation and its proper officers and directors or their designees shall be authorized to execute and deliver, in the name and on behalf of the Company or Merger Sub, all such deeds, bills of sale, assignments and assurances and do, in the name and on behalf of the Company or Merger Sub, all such other acts and things necessary, desirable or proper to vest, perfect or confirm its right, title or interest in, to or under any of the properties, rights, privileges, powers, franchises or assets of the Company or Merger Sub, as applicable, and otherwise to carry out the purposes of this Agreement.

## ARTICLE II
## EFFECTS OF THE MERGER; CONSIDERATION

Section 2.1 Conversion of Company Securities.

At the Effective Time, by virtue of the Merger and without any action on the part of the Company, Merger Sub, Buyer, the Stockholders, the Warrant Holders or the Option Holders:

(a) Each share of common stock of Merger Sub issued and outstanding immediately prior to the Effective Time shall be converted into and become one validly issued, fully paid and nonassessable share of common stock of the Surviving Corporation.

(b) Each share of Common Stock, together with the related Right attached thereto, that is owned by (i) the Company as treasury stock or (ii) any wholly owned Subsidiary of the Company, shall be canceled without any conversion thereof and no payment or distribution shall be made with respect thereto.

(c) Except as otherwise provided in clause (b) above and subject to Section 2.4, each share of Common Stock outstanding immediately prior to the Effective Time, together with the related Right attached thereto, shall be converted into the right to receive $8.10 in cash, payable to the holder thereof, without interest (the "**Common Stock Consideration**"). All shares of Common Stock converted into the right to receive the Common Stock Consideration pursuant to this Section 2.1(c) shall cease to be outstanding as of the Effective Time, and shall be cancelled and retired and shall cease to exist, and each holder of a certificate that immediately prior to the Effective Time represented shares of Common Stock, together with the related Rights, shall thereafter cease to have any rights with respect to such shares or to such related Rights, except the right to receive the Common Stock Consideration to be issued in consideration therefor upon the surrender of such certificate.

(d) Each Warrant issued and outstanding immediately prior to the Effective Time shall be converted as of the Effective Time into the right to receive a sum in cash equal to such Warrant's Warrant Cancellation Payment, without interest, and all such Warrants shall no longer be outstanding and shall automatically be cancelled and shall cease to exist, and each former Warrant Holder shall cease to have any rights with respect thereto, other than the right to receive the Warrant Cancellation Payment in respect of each Warrant held by such Warrant Holder as set forth herein. The Company shall use its commercially reasonable efforts to take all actions necessary to effectuate the foregoing.

(e) Each Option issued and outstanding immediately prior to the Effective Time, whether or not then exercisable, shall be converted immediately after giving effect to the Effective Time into the right to receive, as promptly as practicable after the Effective Time, a sum in cash equal to such Option's Option Cancellation Payment, without interest, and all such Options shall no longer be outstanding and shall automatically be cancelled and shall cease to exist, and each former Option Holder shall cease to have any rights with respect thereto, other than the right to receive the Option Cancellation Payment in respect of each Option held by such Option Holder as set forth herein. Notwithstanding anything to the contrary contained in this Agreement, if the exercise price per share of Common Stock of any Option is equal to or greater than the Common Stock Consideration, such Option shall be cancelled without any cash payment being made in respect thereof. The Company shall use its commercially reasonable efforts to take all actions necessary to effectuate the foregoing. As of the Effective Time, the Stock Plans shall terminate and all rights under any provision of any other plan, program or arrangement of the Company or any Subsidiary of the Company providing for the issuance or grant of any other interest in respect of the capital stock of the Company or any Subsidiary of the Company shall be cancelled.

(f) The Common Stock Consideration and amount of the Option Cancellation Payments and Warrant Cancellation Payments payable pursuant to Section 2.1(c), (d) and (e), respectively, have been calculated based upon the representations and warranties made by the Company in Section 3.3. Without limiting the effect of the failure of the representations and warranties made by the Company in Section 3.3 to be true and correct, in the event that, at the Effective Time, the actual number of shares of Common Stock and other shares of capital stock of the Company outstanding or the actual number of shares of capital stock of the Company issuable upon the exercise of outstanding Options, Warrants or similar agreements or upon conversion of securities (including without limitation, as a result of any stock split, stock dividend, including any dividend or distribution of securities convertible into Shares, or recapitalization) is greater than as described in Section 3.3 (including the exercise or conversion of any currently outstanding Options, Warrants or similar agreements described in Section 3.3), the Common Stock Consideration, Option Cancellation Payments and Warrant Cancellation Payments payable as contemplated herein shall be adjusted downward, but only to the extent necessary to ensure that the aggregate amount of the Common Stock Consideration and amounts payable in respect of Option Cancellation Payments and Warrant Cancellation Payments shall not exceed the sum of: (i) $247,175,000 plus (ii) an amount equal to (A) $8.10 multiplied by (B) the number of shares of Common Stock issued as the result of the exercise of any currently outstanding Options or Warrants prior to the Effective Time, plus (iii) $3,835,077, less for each share of Common Stock described in clause (ii) above, the difference between $8.10 and the exercise price paid to the Company upon the exercise of the Option or Warrant pursuant to which such share is issued.

Section 2.2 Exchange Procedures.

(a) Prior to the Effective Time, Buyer shall appoint the Paying Agent to act as agent for the holders of shares of Common Stock and Warrants in connection with the Merger and to receive the funds to which such holders shall become entitled pursuant to this Article II.

(b) Promptly following the Effective Time, the Surviving Corporation shall cause to be mailed, or otherwise make available, to each holder of record of Certificates entitled to receive consideration pursuant to Section 2.1 the form of Letter of Transmittal. After the Effective Time, each holder of certificates or other instruments formerly evidencing shares of Common Stock or Warrants (the "**Certificates**"), upon surrender of such Certificates to the Paying Agent, together with a properly completed Letter of Transmittal and such other documents as may be reasonably required by the Paying Agent, shall be entitled to receive from the Paying Agent, in exchange therefor, the aggregate consideration for such shares of Common Stock or Warrants as set forth herein, as the case may be, in cash as contemplated by this Agreement, and the Certificates so surrendered shall be cancelled. Until surrendered as contemplated by this Section 2.2 (other than Certificates representing Dissenting Shares), each Certificate shall be deemed at any time after the Effective Time to represent only the right to receive the aggregate consideration for such shares of Common Stock or Warrants, as the case may be, in cash as contemplated by this Agreement, without interest thereon. All cash consideration delivered upon the surrender of

Certificates in accordance with the terms of this Section 2.2 shall be deemed to have been paid in full satisfaction of all rights pertaining to shares of Common Stock and Warrants theretofore represented by such Certificates.

(c) If any Certificate shall have been lost, stolen or destroyed, upon the making of an affidavit of that fact by the Person claiming such Certificate to be lost, stolen or destroyed and, if required by the Buyer, the posting by such Person of a bond or other surety in such amount as the Buyer may reasonably direct as indemnity against any claim that may be made with respect to such Certificate and subject to such other reasonable conditions as the Buyer may impose, the Paying Agent shall deliver in exchange for such Certificate the consideration into which shares of Common Stock or Warrants theretofore represented by such Certificate shall have been converted pursuant to this Article II.

(d) If any payment under this Article II is to be made to a Person other than the Person in whose name any Certificate surrendered in exchange therefor is registered, it shall be a condition of payment that the Certificate so surrendered shall be properly endorsed or otherwise in proper form for transfer and that the Person requesting such payment shall pay any transfer or other similar Taxes required by reason of the payment to a Person other than the registered holder of the Certificate surrendered or such Person shall establish to the satisfaction of the Surviving Corporation that such Taxes have been paid or are not applicable.

(e) None of Buyer, Merger Sub or the Surviving Corporation shall be liable to any Person in respect of any cash delivered to a public official pursuant to any applicable abandoned property, escheat or similar Law. At any time following the expiration of one (1) year after the Effective Time, the Surviving Corporation shall, in its sole discretion, be entitled to require the Paying Agent to deliver to it any funds (including any interest received with respect thereto) that had been made available to the Paying Agent and that have not been disbursed to holders of Certificates, and such funds shall thereafter become the property of the Surviving Corporation. Such funds may be commingled with the general funds of the Surviving Corporation and shall be free and clear of any claims or interests of any Person. Thereafter, such holders shall be entitled to look to the Surviving Corporation (subject to any applicable abandoned property, escheat or similar Law) only as general creditors thereof with respect to the applicable consideration payable as contemplated by this Agreement (net of any amounts that would be subject to withholding) upon due surrender of their Certificates, without any interest thereon.

(f) At the Effective Time, the stock transfer books of the Company shall be closed, and there shall be no further registration of transfer in the stock transfer books of the Surviving Corporation of the shares of Common Stock, Warrants or Options, as the case may be, that were outstanding immediately prior to the Effective Time. If, after the Effective Time, Certificates are presented to the Surviving Corporation or the Paying Agent for any reason, they shall be canceled and exchanged as provided in this Section 2.2.

(g) As soon as practicable following the Effective Time, the Surviving Corporation shall, in exchange for the Options that became entitled to receive the consideration specified in Section 2.1, make the Option Cancellation Payment in respect of each such Option to each Option Holder.

Section 2.3 Deposit at Closing.

At the Closing, Buyer shall deposit (or cause to be deposited) with the Paying Agent, for exchange and payment in accordance with this Article II, an amount equal to the sum of *(x)* the aggregate Common Stock Consideration and *(y)* the aggregate Warrant Cancellation Payments. The Paying Agent shall invest funds held by it for purposes of this Article II as directed by Buyer, on a daily basis. Any interest or other income resulting from such investments shall be paid to Buyer.

Section 2.4 Dissenting Shares.

(a) Notwithstanding any provision of this Agreement to the contrary, shares of the Company's capital stock that are outstanding immediately prior to the Effective Time and that are held by holders who shall not have voted in favor of the Merger or consented thereto in writing and who shall have demanded properly in writing appraisal for such shares in accordance with Section 262 of the DGCL (collectively, the "**Dissenting Shares**") shall not be converted into or represent the right to receive the consideration set forth in Section 2.1. Such holders shall be entitled to receive such consideration as is determined to be due with respect to such Dissenting Shares in accordance with the provisions of Section 262 of the DGCL, except that all Dissenting Shares held by holders who shall have failed to perfect or who effectively shall have withdrawn or lost their rights to appraisal of such shares under Section 262 of the DGCL shall thereupon be deemed to have been converted into and to have become exchangeable for, as of the Effective Time, the right to receive the consideration specified in Section 2.1, without any interest thereon, upon surrender, in the manner provided in Section 2.2, of the certificate or certificates that formerly evidenced such Dissenting Shares.

(b) The Company shall deliver to Buyer prompt written notice of any demands for appraisal received by the Company, withdrawals of such demands and any other instruments served pursuant to the DGCL and received by the Company, and the Company shall afford Buyer the opportunity to direct all negotiations and proceedings with respect to demands for appraisal under the DGCL. The Company shall not, except with the prior written consent of Buyer, make any payment with respect to any demands for appraisal or offer to settle or settle any such demands.

Section 2.5 Tax Withholding.

The Surviving Corporation and Buyer shall be entitled to deduct and withhold, or to cause the Paying Agent to deduct and withhold (consistent with the Company's past practice), from the consideration otherwise payable pursuant to this Agreement to or for the benefit of any holder of any shares of Common Stock, Options or Warrants such amounts as it is required to deduct and withhold with respect to the making of such payment under the Code or any provision of state, local, or foreign tax law. To the extent that amounts are so withheld, such withheld amounts shall be treated for all purposes of this Agreement as having been paid to the holder of shares of Common Stock, Options or Warrants in respect of which such deduction or withholding was made, and the Surviving Corporation or Buyer, as applicable, shall properly and timely remit any such withheld amounts to the appropriate Governmental Entity.

## ARTICLE III
## REPRESENTATIONS AND WARRANTIES OF THE COMPANY

Except as set forth in the Disclosure Letter delivered by the Company prior to, or concurrently with, the execution of this Agreement (the “**Disclosure Letter**”), or, to the extent the qualifying nature of such disclosure with respect to a specific representation or warranty is readily apparent therefrom, as set forth in the Company SEC Reports filed on or after January 1, 2006 and prior to the date hereof (without regard to the exhibits thereto or items included therein that are incorporated by reference to Company SEC Reports filed by the Company prior to January 1, 2006), the Company hereby represents and warrants to Buyer and Merger Sub as follows:

Section 3.1 Organization, Standing and Power.

Each of the Company and its Subsidiaries is a corporation duly organized, validly existing and in good standing under the laws of its jurisdiction of incorporation and has all requisite corporate power and authority to own, lease and operate its properties and assets and to carry on its business as now being conducted. Each of the Company and its Subsidiaries is duly licensed or qualified to do business and is in good standing in each jurisdiction in which such qualification or licensing is necessary because of the property and assets owned, leased or operated by it or because of the nature of its business as now being conducted, except for any failure to so qualify or be licensed or in good standing that, individually or in the aggregate, would not reasonably be expected to have a Company Material Adverse Effect. Section 3.1 of the Disclosure Letter lists the jurisdictions of incorporation and foreign qualifications of the Company and each of its Subsidiaries. The Company has made available to Buyer true, complete and correct copies of the constitutive documents of each of the Company and its Subsidiaries, in each case as amended to the date of this Agreement, and has made available to Buyer each such entity’s minute books and stock records. Neither the Company nor any of its Subsidiaries is in violation of any provision of its respective certificate or articles of incorporation, by-laws or similar constitutive document. Section 3.1 of the Disclosure Letter contains a true and correct list of the directors and officers of each of the Company and its Subsidiaries as of the date of this Agreement.

Section 3.2 Authority; Approvals.

(a) The execution, delivery and performance of this Agreement by the Company and the consummation of the transactions contemplated hereby are within its corporate powers and authority and have been duly and validly authorized by all necessary corporate action on the part of the Company (other than the adoption of this Agreement by the Required Company Stockholders). This Agreement has been duly and validly executed and delivered by the Company, and (assuming due authorization, execution and delivery by Buyer and Merger Sub) constitutes the valid and binding obligation of the Company, enforceable against the Company in accordance with its terms, except as such enforceability may be limited by bankruptcy, insolvency, reorganization, moratorium and other similar laws of general applicability relating to or affecting creditor's rights generally and by the application of general principles of equity.

(b) The Board of Directors of the Company (the "**Company Board**") has unanimously (i) determined that this Agreement and the Merger are fair to, and in the best interests of, the Company and its stockholders; (ii) resolved that the Merger is fair to, and in the bests interests of, the Company and its stockholders and declared this Agreement and the Merger to be advisable; (iii) resolved to approve this Agreement; and (iv) resolved to recommend that the Company's stockholders adopt this Agreement, and, as of the date hereof, none of the aforesaid actions by the Board of Directors of the Company has been amended, rescinded or modified.

(c) The affirmative vote of the holders of a majority of outstanding shares of Common Stock (the "**Required Company Stockholders**") is the only vote of the holders of any class or series of the Company's capital stock necessary to approve the Merger.

Section 3.3 Capitalization.

(a) The authorized capital stock of the Company consists of 100,000,000 shares of Common Stock and 5,000,000 shares of preferred stock, par value $0.01 per share (the "**Preferred Stock**"). As of the date of this Agreement, (i) 30,508,638 shares of Common Stock, including the associated Rights, were issued and outstanding (none of which are shares of Restricted Stock); (ii) 1,333,683 shares of Common Stock are held in the treasury of the Company; (iii) no shares of Common Stock are held by Subsidiaries of the Company; and (iv) no shares of Preferred Stock are outstanding.

(b) Section 3.3(b)(i) of the Disclosure Letter sets forth a true and correct list of all of the Company's Subsidiaries, together with their respective authorized capital stock, number of shares issued and outstanding and record ownership of such shares. Except as set forth in Section 3.3(b)(ii) of the Disclosure Letter, the Company does not have any Subsidiaries or own or hold, directly or indirectly, any Capital Securities of, or has made any investment, in any other Person. Except as set forth in Section 3.3(b) of the Disclosure Letter, all issued and outstanding shares of capital stock of the Company's Subsidiaries have been duly authorized, were validly issued, are fully paid and nonassessable and subject to no preemptive rights and are directly or indirectly owned beneficially and of record by the Company, free and clear of all Encumbrances, and free of any other limitation or restriction (including any restriction on the right to vote, sell or otherwise dispose of such Capital Securities).

(c) Except for (i) issued and outstanding Common Stock referenced in Sections 3.3(a)(i) and 3.3(a)(ii); (ii) 4,984,060 shares of Common Stock reserved for issuance upon exercise of Options, as described in Section 3.3(d) of the Disclosure Letter; (iii) 150,000 shares of Common Stock reserved for issuance upon exercise of the Warrants, as described in Section 3.3(e) of the Disclosure Letter; (iv) the shares of Preferred Stock designated as "**Series A Preferred Stock**" reserved for issuance in accordance with the Rights Agreement; and (v) as set forth in Sections 3.3(b) of the Disclosure Letter, at the time of execution of this Agreement, no shares of capital stock or other voting securities of the Company or any of its Subsidiaries are issued, reserved for issuance or outstanding. All outstanding shares of capital stock of the Company have been duly authorized, were validly issued, are fully paid and nonassessable and subject to no preemptive rights. Except for the Common Stock, there are no bonds, debentures, notes or other indebtedness or securities of the Company or any of its Subsidiaries having the right to vote (or convertible into, or exchangeable for, securities having the right to vote) on any matters on which stockholders of the Company or such Subsidiary may vote. Except for the Options, Warrants and Rights, there are no securities, options, warrants, calls, rights, commitments, agreements, arrangements or undertakings of any kind to which the Company or any of its Subsidiaries is a party relating to the issued or unissued Capital Securities of the Company or any Subsidiary. Except for the Options, Warrants and Rights, there are no securities, options, warrants, calls, rights, commitments, agreements, arrangements or undertakings of any kind to which the Company or any of its Subsidiaries is a party or by which any such Person is bound obligating such Person to issue, deliver or sell, or cause to be issued, delivered or sold, additional shares of Capital Securities of the Company or any of its Subsidiaries or obligating such Person to issue, grant, extend or enter into any such security, option, warrant, call right, commitment, agreement, arrangement or undertaking. There are no outstanding rights, commitments, agreements, arrangements or undertakings of any kind obligating the Company or any of its Subsidiaries (i) to repurchase, redeem or otherwise acquire any Capital Securities of the Company or any of its Subsidiaries or any securities of the type described in this Section 3.3(c) or (ii) to purchase or otherwise acquire any Capital Securities of any other Person. No Restricted Stock is outstanding, and no stock appreciation rights have been issued by the Company or any of its Subsidiaries.

(d) The names of the optionee of each Option, the date of grant of each Option, the number of shares subject to each such Option, the expiration date of each such Option, and the price at which each such Option may be exercised are set forth in Section 3.3(d) of the Disclosure Letter. No option that became vested and exercisable on or after January 1, 2005 was granted with an exercise price per share that was less than the per share fair market value of the Company Common Stock underlying such Option on the grant date thereof.

(e)