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Davis Wright Tremaine LLP

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2600 CENTURY SQUARE
1501 FOURTH AVENUE
SEATTLE, WA 98101-1688

TEL (206) 622-3150
FAX (206) 628-7699
www.dwt.com

DEPOSIT D190 · DATE AUG 19 1999

SHELLEY HALL
Direct (206) 622-3150
Shelleyhall@dwt.com

August 5, 1999

991154-TI

Florida Public Service Commission
Division of Records and Reporting
2540 Shumard Oak Blvd.
Tallahassee, Florida 32399-0850

RE: Application of NEXTLINK Long Distance Services, Inc. for Authority to Provide Interexchange Telecommunications Service

Dear Sir or Madam:

NEXTLINK Long Distance Services, Inc., by its attorneys, presents an original and six (6) copies of this cover letter and the enclosed Application Form, including an initial tariff. This packet also includes a $250 filing fee.

... is enclosed to be date-stamped and returned to us in the self-

DAVIS WRIGHT TREMAINE LLP
Law Offices
2600 Century Square 1501 Fourth Avenue
Seattle Washington 98101-1688

Seafirst Bank
Disbursement Account
First Union National Bank
Chapel Hill, NC

No. 535838

66-156/531

DATE August 17 1999

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FLORIDA PUBLIC SERVICE COMMISSION
RECORDS AND REPORTING DIVISION
2540 SHUMARD OAK BLVD.
TALLAHASSEE, FL. 32399-0850

DAVIS WRIGHT TREMAINE LLP

BY

09904-99

Checks Exceeding $50,000 Require Two Signatures

STATE OF FLORIDA

DIVISION OF RECORDS & REPORTING
BLANCA S. BAYÓ
DIRECTOR
(850) 413-6770

Public Service Commission

August 19, 1999

Shelby Hall, Attorney
Davis Wright Tremaine LLP
2600 Century Square
1501 Fourth Avenue
Seattle, Washington 98101-1688

Re: Docket No. 991154-TI

Dear Mr. Hall:

This will acknowledge receipt of an application for certificate to provide interexchange telecommunications service by NEXTLINK Long Distance Services, Inc., which was filed with this office on August 19, 1999 and assigned the above-referenced docket number. Appropriate staff members will be advised.

Mediation may be available to resolve any dispute in this docket. If mediation is conducted, it does not affect a substantially interested person's right to an administrative hearing. For more information, contact the Office of General Counsel at (850) 413-6078 or FAX (850) 413-6079.

Please make notes as well that Commission Rule 25-22.005(7), F.A.C., requires certificated companies to notify the Commission of any changes in name, telephone, address, or contact person. Should your application be granted by the Commission, you will be expected to comply with this rule by advising us of any changes as they occur.

Division of Records and Reporting
Florida Public Service Commission

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SHELLEY HALL
Direct (206) 622-3150
Shelleyhall@dwt.com

August 5, 1999

Florida Public Service Commission
Division of Records and Reporting
2540 Shumard Oak Blvd.
Tallahassee, Florida 32399-0850

991154-TI

RE: Application of NEXTLINK Long Distance Services, Inc. for Authority to Provide Interexchange Telecommunications Service

Dear Sir or Madam:

NEXTLINK Long Distance Services, Inc., by its attorneys, presents an original and six (6) copies of this cover letter and the enclosed Application Form, including an initial tariff. This packet also includes a $250 filing fee.

An extra copy of this filing is enclosed to be date-stamped and returned to us in the self-addressed, postage paid envelope enclosed. If you have any questions regarding this filing, please contact the undersigned.

Respectfully submitted,

DAVIS WRIGHT TREMAINE LLP

Shelley Hall

Shelley Hall

Check received with filing and forwarded to Fiscal for deposit. Fiscal to forward a copy of check to RAR with proof of deposit.

Initials of person who forwarded check:

DOCUMENT NUMBER-DATE
09904 AUG 19 99
FPSC-RECORDS/REPORTING

F:\DOCS\38936\149\Long Distance Certs\Florida letter.doc
Seattle

** **FLORIDA PUBLIC SERVICE COMMISSION** **

DIVISION OF TELECOMMUNICATIONS
BUREAU OF CERTIFICATION AND SERVICE EVALUATION

Application Form for Authority to Provide
Interexchange Telecommunications Service
Between Points Within the State of Florida

Instructions

- This form is used as an application for an original certificate and for approval of assignment or transfer of an existing certificate. In the case of an assignment or transfer, the information provided shall be for the assignee or transferee (See Appendix A).

- Print or Type all responses to each item requested in the application and appendices. If an item is not applicable, please explain why.

- Use a separate sheet for each answer which will not fit the allotted space.

- Once completed, submit the original and six (6) copies of this form along with a non-refundable application fee of **$250.00** to:

  Florida Public Service Commission
  Division of Records and Reporting
  2540 Shumard Oak Blvd.
  Tallahassee, Florida 32399-0850
  (850) 413-6770

  Note: **No filing fee is required** for an assignment or transfer of an existing certificate to another certificated company.

- If you have questions about completing the form, contact:

  Florida Public Service Commission
  Division of Telecommunications
  Bureau of Certification and Service Evaluation
  2540 Shumard Oak Blvd.
  Tallahassee, Florida 32399-0850
  (850) 413-6600

DOCUMENT NUMBER-DATE
09904 AUG 19 98
FPSC-RECORDS/REPORTING

1. This is an application for ✓ (check one):

   (X) **Original certificate** (new company).

   ( ) **Approval of transfer of existing certificate:** Example, a certificated company purchases an existing certificated company and desires to retain the authority of both certificates.

   ( ) **Approval of assignment of existing certificate:** Example, a non-certificated company purchases an existing company and desires to retain the certificate of authority rather than apply for a new certificate.

   ( ) **Approval of transfer of control:** Example, a company purchases 51% of a certificated company. The Commission must approve the new controlling entity.

2. Name of company:

   NEXTLINK Long Distance Services, Inc.

3. Name under which applicant will do business (fictitious name, etc.):

   NEXTLINK Long Distance Services, Inc.

4. Official mailing address (including street name & number, post office box, city, state, zip code):

   500 108th Ave. NE, Ste. 2200

   Bellevue, WA 98004

5. Florida address (including street name & number, post office box, city, state, zip code):

   Registered Agent: Corporation Service Company

   1201 Hays Street, Tallahassee, FL 32301

6. Select type of business your company will be conducting ✓ (check all that apply):

   (X) **Facilities-based carrier** - company owns and operates or plans to own and operate telecommunications switches and transmission facilities in Florida.

(X) **Operator Service Provider** - company provides or plans to provide alternative operator services for IXCs; or toll operator services to call aggregator locations; or clearinghouse services to bill such calls.

(X) **Reseller** - company has or plans to have one or more switches but primarily leases the transmission facilities of other carriers. Bills its own customer base for services used.

( ) **Switchless Rebiller** - company has no switch or transmission facilities but may have a billing computer. Aggregates traffic to obtain bulk discounts from underlying carrier. Rebills end users at a rate above its discount but generally below the rate end users would pay for unaggregated traffic.

( ) **Multi-Location Discount Aggregator** - company contracts with unaffiliated entities to obtain bulk/volume discounts under multi-location discount plans from certain underlying carriers, then offers resold service by enrolling unaffiliated customers.

(X) **Prepaid Debit Card Provider** - any person or entity that purchases 800 access from an underlying carrier or unaffiliated entity for use with prepaid debit card service and/or encodes the cards with personal identification numbers.

7. Structure of organization:

( )	Individual	( )	Corporation
(X)	Foreign Corporation	( )	Foreign Partnership
( )	General Partnership	( )	Limited Partnership
( )	Other ______		

8. **If individual**, provide: **NOT APPLICABLE**

Name:______

Title:______

Address:______

City/State/Zip:______

Telephone No.:______ **Fax No.:**______

Internet E-Mail Address:______

Internet Website Address:______

9. **If incorporated in Florida,** provide proof of authority to operate in Florida: **NOT APPLICABLE**

   (a) **The Florida Secretary of State Corporate Registration number:**

   ____

10. **If foreign corporation,** provide proof of authority to operate in Florida:

    (a) **The Florida Secretary of State Corporate Registration number:**

    F99000003166 PLEASE SEE SUPPLEMENT FOR PROOF OF AUTHORITY.

11. **If using fictitious name-d/b/a,** provide proof of compliance with fictitious name statute (Chapter 865.09, FS) to operate in Florida: **NOT APPLICABLE**

    (a) **The Florida Secretary of State fictitious name registration number:**

    ______

12. **If a limited liability partnership,** provide proof of registration to operate in Florida: **NOT APPLICABLE**

    (a) **The Florida Secretary of State registration number:**

13. **If a partnership,** provide name, title and address of all partners and a copy of the partnership agreement. **NOT APPLICABLE**

    Name:______________________________

    Title:______________________________

    Address:______________________________

    City/State/Zip:______________________________

    Telephone No.:__________________ **Fax No.:**__________________

    Internet E-Mail Address:______________________________

    Internet Website Address:______________________________

14. **If a foreign limited partnership,** provide proof of compliance with the foreign limited partnership statute (Chapter 620.169, FS), if applicable. **NOT APPLICABLE.**

    (a) **The Florida registration number:**______________________________

15. Provide **F.E.I. Number** (if applicable): **91-1957034**

16. Provide the following (if applicable):

(a) Will the name of your company appear on the bill for your services?

(x) Yes ( ) No

(b) If not, who will bill for your services? **NOT APPLICABLE**

Name:

Title:

Address:

City/State/Zip:

Telephone No.: **Fax No.:**

(c) How is this information. provided?

APPLICANT WILL BILL CUSTOMERS DIRECTLY

17. Who will receive the bills for your service?

( )	Residential Customers	(X)	Business Customers
( )	PATs providers	( )	PATs station end-users
( )	Hotels & motels	( )	Hotel & motel guests
( )	Universities	( )	Universities dormitory residents

( ) Other: (specify:)

18. Who will serve as liaison to the Commission with regard to the following?

(a) The application:

Name: Shelley Hall

Title: Counsel for NEXTLINK Long Distance Services, Inc.

Address: DAVIS WRIGHT TREMAINE LLP, 2600 Century Square, 1501 Fourth Avenue

City/State/Zip: Seattle, WA 98101-1688

Telephone No.: (206) 622-3150 Fax No.: (206) 628-7699

Internet E-Mail Address: shelleyhall@dwt.com

Internet Website Address:

(b) Official point of contact for the ongoing operations of the company:

Name: Doug Kinkoph

Title:

NEXTLINK Long Distance Services, Inc.

Address: Two Easton Oval, Ste. 300

City/State/Zip: Columbus, Ohio 43219

Telephone No.: (614) 629-3200 Fax No.: (614) 629-3201

Internet E-Mail Address: dkinkoph@nextlink.net

Internet Website Address:

(c) Complaints/Inquiries from customers:

Name: Applicant will handle complaints and inquiries through a toll-free number listed below.

Title:

Address:

City/State/Zip:

Telephone No.: 1 (800) 900-6398 Fax No.:

Internet E-Mail Address:

Internet Website Address:

19. List the states in which the applicant:

(a) has operated as an interexchange telecommunications company.

Applicant has not operated as an interexchange telecommunications company in any state.

(b) has applications pending to be certificated as an interexchange telecommunications company.

Applicant has applications pending in Louisiana, Kentucky, Kansas, Vermont, Oklahoma, Alaska and Oregon.

(c) is certificated to operate as an interexchange telecommunications company.

Applicant is certified to operate as an interexchange telecommunicatons company in Arkansas, Montana and Rhode Island.

(d) has been denied authority to operate as an interexchange telecommunications company and the circumstances involved.

Applicant has not been denied authority in any state.

(e) has had regulatory penalties imposed for violations of telecommunications statutes and the circumstances involved.

Applicant has not had any regulatory penalties imposed.

(f) has been involved in civil court proceedings with an interexchange carrier, local exchange company or other telecommunications entity, and the circumstances involved.

Applicant has not been involved in civil court proceedings with an interexchange carrier local exchange company or other telecommunications entity.

20. Indicate if any of the officers, directors, or any of the ten largest stockholders have previously been:

(a) adjudged bankrupt, mentally incompetent, or found guilty of any felony or of any crime, or whether such actions may result from pending proceedings. If so, please explain.

None of the officers or directors of applicant have been adjudged bankrupt, mentally incompetent or found guilty of any felony or of any crime.

(b) an officer, director, partner or stockholder in any other Florida certificated telephone company. If yes, give name of company and relationship. If no longer associated with company, give reason why not.

Yes, officers and directors of applicant also are officers and directors NEXTLINK Florida, Inc. NEXTLINK Communications, Inc. wholly owns both NEXTLINK Florida, Inc. and applicant.

21. The applicant will provide the following interexchange carrier services ✓ (check all that apply):

(a) ______ **MTS with distance sensitive per minute rates**

- ______ Method of access is FGA
- ______ Method of access is FGB
- ______ Method of access is FGD
- ______ Method of access is 800

(b) ______ **MTS with route specific rates per minute**

- ______ Method of access is FGA
- ______ Method of access is FGB
- ______ Method of access is FGD
- ______ Method of access is 800

(c) X ______ **MTS with statewide flat rates per minute (i.e. not distance sensitive)**

- ______ Method of access is FGA
- ______ Method of access is FGB
- X ______ Method of access is FGD
- ______ Method of access is 800

(d) ______ **MTS for pay telephone service providers**

(e) ______ **Block-of-time calling plan (Reach Out Florida, Ring America, etc.).**

(f) X____ **800 service (toll free)**

(g) X____ **WATS type service (bulk or volume discount)**

X____ Method of access is via dedicated facilities
X____ Method of access is via switched facilities

(h) X____ **Private line services (Channel Services)**
(For ex. 1.544 mbs., DS-3, etc.)

(i) X____ **Travel service**

______ Method of access is 950
X____ Method of access is 800

(j) ______ 900 service

(k) X____ Operator services

X________ Available to presubscribed customers
X________ Available to non presubscribed customers (for example, to patrons of hotels, students in universities, patients in hospitals).
_________ Available to inmates

l. Services included are:

X________ Station assistance
X________ Person-to-person assistance
X________ Directory assistance
_________ Operator verify and interrupt
X________ Conference calling

22. Submit the proposed tariff under which the company plans to begin operation. Use the format required by Commission Rule 25-24.485 (example enclosed). **SEE SUPPLEMENT FOR TARIFF.**

23. Submit the following:

A. Financial capability. SEE ATTACHED SUPPLEMENT.

The application **<u>should contain</u>** the applicant's audited financial statements for the most recent 3 years. If the applicant does not have audited financial statements, it shall so be stated.

The unaudited financial statements should be signed by the applicant's chief executive officer and chief financial officer affirming that the financial statements are true and correct and should include:

1. the balance sheet;

2. income statement; and

3. statement of retained earnings.

NOTE: *This documentation may include, but is not limited to, financial statements, a projected profit and loss statement, credit references, credit bureau reports, and descriptions of business relationships with financial institutions.*

Further, the following (which includes supporting documentation) should be provided:

1. **A written explanation** that the applicant has sufficient financial capability to provide the requested service in the geographic area proposed to be served.

2. **A written explanation** that the applicant has sufficient financial capability to maintain the requested service.

3. **A written explanation** that the applicant has sufficient financial capability to meet its lease or ownership obligations.

B. Managerial capability; give resumes of employees/officers of the company that would indicate sufficient managerial experiences of each. **SEE ATTACHED SUPPLEMENT.**

C. Technical capability; give resumes of employees/officers of the company that would indicate sufficient technical experiences or indicate what company has been contracted to conduct technical maintenance. **SEE ATTACHED SUPPLEMENT.**

** APPLICANT ACKNOWLEDGMENT STATEMENT **

1. **REGULATORY ASSESSMENT FEE:** I understand that all telephone companies must pay a regulatory assessment fee in the amount of .15 of one percent of its gross operating revenue derived from intrastate business. Regardless of the gross operating revenue of a company, a minimum annual assessment fee of $50 is required.

2. **GROSS RECEIPTS TAX:** I understand that all telephone companies must pay a gross receipts tax of two and one-half percent on all intra and interstate business.

3. **SALES TAX:** I understand that a seven percent sales tax must be paid on intra and interstate revenues.

4. **APPLICATION FEE:** I understand that a non-refundable application fee of $250.00 must be submitted with the application.

UTILITY OFFICIAL:

R Gerard Salemme — 7-30-99

Signature — Date

R. Gerard Salemme

Title: **Sr. Vice President, External Affairs And Industry Relations** — Telephone No.

Address: **500 108th Ave. NE, Ste. 2200**
Bellevue, WA 98004 — Fax No.

ATTACHMENTS:

A - CERTIFICATE SALE, TRANSFER, OR ASSIGNMENT STATEMENT
B - CUSTOMER DEPOSITS AND ADVANCE PAYMENTS
C - CURRENT FLORIDA INTRASTATE NETWORK
D - AFFIDAVIT

**** APPENDIX A ****

CERTIFICATE TRANSFER, OR ASSIGNMENT STATEMENT

I, (Name) **NOT APPLICABLE** ____________________

(Title) ____ of

____

(Name of Company)

and current holder of Florida Public Service Commission Certificate Number #____________________, have reviewed this application and join in the petitioner's request for a:

( ) transfer

( ) assignment

of the above-mentioned certificate.

UTILITY OFFICIAL

____________________ ____________________

Signature Date

____________________ ____________________

Title Telephone No.

Address: ____________________ ____________________

Fax No.

____

____

**** APPENDIX B ****

CUSTOMER DEPOSITS AND ADVANCE PAYMENTS

A statement of how the Commission can be assured of the security of the customer's deposits and advance payments may be provided in one of the following ways (applicant, please √ check one):

(**X**) The applicant will **not** collect deposits nor will it collect payments for service more than one month in advance.

(__) The applicant intends to collect deposits and/or advance payments for more than one month's service and will file and maintain a surety bond with the Commission in an amount equal to the current balance of deposits and advance payments in excess of one month. (The bond must accompany the application.) **Applicant is submitting a $5,000 bond.**

UTILITY OFFICIAL

7-30-99

Signature: **R. Gerard Salemme** Date

Sr. Vice President, External Affairs and Industry Relations

Title Telephone No.

Address: **500 108th Ave., NE, Ste. 2200**

Fax No.

Bellevue, WA 98004

** APPENDIX C **

CURRENT FLORIDA INTRASTATE SERVICES

Applicant **has** (   ) or **has not** (**X**) previously provided intrastate telecommunications in Florida.

If the answer is has, fully describe the following:

a) What services have been provided and when did these services begin?

NOT APPLICABLE

b) If the services are not currently offered, when were they discontinued?

NOT APPLICABLE

UTILITY OFFICIAL

Signature

Date: 7-30-99

R. Gerard Salemme

Telephone No.

Title: **Sr. Vice President, External Affairs and Industry Relations**

Address: **500 108th Ave., NE, Ste. 2200**

Fax No.

Bellevue, WA 98004

** APPENDIX D **

AFFIDAVIT

By my signature below, I, the undersigned officer, attest to the accuracy of the information contained in this application and attached documents and that the applicant has the technical expertise, managerial ability, and financial capability to provide alternative local exchange company service in the State of Florida. I have read the foregoing and declare that, to the best of my knowledge and belief, the information is true and correct. I attest that I have the authority to sign on behalf of my company and agree to comply, now and in the future, with all applicable Commission rules and orders.

Further, I am aware that, pursuant to Chapter 837.06, Florida Statutes, "Whoever knowingly makes a false statement in writing with the intent to mislead a public servant in the performance of his official duty shall be guilty of a misdemeanor of the second degree, punishable as provided in s. 775.082 and s. 775.083."

UTILITY OFFICIAL

Signature 7-30-99
Date

R. Gerard Salemme

Title: **Sr. Vice President, External Affairs and Industry Relations**

Telephone No.

Address: **500 108th Ave., NE, Ste. 2200**

Bellevue, WA 98004

Fax No.

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF FLORIDA
BUREAU OF CERTIFICATION AND SERVICE EVALUATION

In the Matter of	)	
	)	
Application of NEXTLINK Long Distance Services, Inc. for a Certificate of Authority to Offer Interexchange Telecommunications Services in the State of Florida	)))))	**Docket No.** **SUPPLEMENT TO APPLICATION**

SUPPLEMENT TO APPLICATION OF NEXTLINK LONG DISTANCE SERVICES FOR A CERTIFICATE OF AUTHORITY

NEXTLINK Long Distance Services, Inc. ("Applicant"), a Washington corporation wholly owned by NEXTLINK Communications, Inc. ("NEXTLINK Communications") hereby submits this Supplemental Application to the Florida Public Service Commission ("Commission") for a Certificate of Authority to operate as a Telecommunications Services Provider offering facilities-based and resold interexchange service throughout Florida. In support of this Application, the following information is provided:

1. ORGANIZATION AND OWNERSHIP OF APPLICANT

NEXTLINK Communications is a telecommunications company founded in 1994 to provide local, long distance and enhanced communications services.[1] NEXTLINK Communications maintains its principal place of business at 500 108th Ave. N.E., Suite 2200, Bellevue, Washington 98004. NEXTLINK Communications is controlled by Eagle River Investments, L.L.C., which in turn is majority owned and controlled by Craig O. McCaw, a

[1] A copy of NEXTLINK Communication's Articles of Incorporation is attached as **Exhibit A**.

leader and pioneer in the telecommunications industry.

Applicant is a corporation organized under the laws of the State of Washington,[2] and is also headquartered at 500 108th Ave. N.E., Suite 2200, Bellevue, Washington 98004. Applicant is a wholly owned subsidiary of NEXTLINK Communications.

2. DESCRIPTION OF SERVICES

Applicant intends to operate as a provider of resold and facilities-based long distance services throughout the state of Florida. Applicant also intends to provide optional pre-paid calling cards in addition to its regular service. Initially, all operator assisted calls will be contracted to third parties. A grant of a Certificate of Authority to the Applicant will benefit the citizens of Florida and the public interest generally by giving customers a source from which to obtain competitive, reliable, and efficient telecommunications services.

3. MANAGERIAL AND TECHNICAL QUALIFICATIONS

The NEXTLINK Communications companies possess the technical and managerial qualifications required to provide telecommunications services throughout the State of Florida. NEXTLINK Communications, through its operating subsidiaries, is certified to provide local and long distance telecommunications services in numerous states.[3] NEXTLINK Communications already operates 26 facilities-based SONET-based fiber optic networks providing local dialtone and long distance services in 41 markets in 14 states. The NEXTLINK Communications

---

[2] A copy of NEXTLINK Long Distance's Articles of Incorporation and its Certificate of Authority to transact business in Florida are attached as **Exhibit B**.

[3] These states are Arizona, California, Colorado, Delaware, Florida, Georgia, Illinois, Indiana, Maryland, Michigan, Missouri, Nevada, New Jersey, New York, North Carolina, Ohio, Pennsylvania, Tennessee, Texas, Utah, Virginia, Washington, Washington D.C. and Wisconsin. Local certification has been obtained in Indiana. Long distance certification has been obtained in Alabama, New Hampshire, New Mexico, Oregon and West Virginia. Local and long distance certification is pending in Mississippi. NEXTLINK Communications has never been denied

companies are managed by an able team of officers who have many years of combined experience in the telephony field.[4] This successful operational experience is evidence of NEXTLINK's technical and managerial capability to deliver the services discussed above in a fashion that is satisfactory to consumers.

4. FINANCIAL QUALIFICATIONS

The NEXTLINK Communications companies also possess adequate financial resources to provide the proposed services. The company is well financed and has sufficient assets.[5] As a wholly owned subsidiary of NEXTLINK Communications, the Applicant will have the financial resources of its parent company available to it.

5. INITIAL TARIFF

Applicant's initial tariff is attached as **Exhibit E**.

6. DEPOSITS/BOND

Applicants may require some customer deposits and, therefore, is submitting a $5,000 bond as requested by the Commission.

7. CONCLUSION

In light of the foregoing, Applicant respectfully submits that the public interest, convenience and necessity would be served by a grant of this Application for a Certificate of Authority to Provide Interexchange Telecommunications Service throughout the State of Florida.

---

authority to offer service in any state.

[4] Brief Biographies of the officers of NEXTLINK Communications are attached as **Exhibit C**. These officers will ultimately be responsible for all Florida operations and may be reached through Applicant's headquarters.

[5] NEXTLINK Communication's Form 10Q for the quarterly period ending September 30, 1998 and its 10KSB for the fiscal year ended December 31, 1997 are attached as **Exhibit D**.

DATED this 6 day of August, 1999.

Respectfully submitted,

NEXTLINK COMMUNICATIONS, INC.
NEXTLINK LONG DISTANCE SERVICES, INC.

By: Shelley Hall

Shelley Hall
DAVIS WRIGHT TREMAINE LLP
2600 Century Square
1501 4th Avenue
Seattle, Washington 98101-1688

Counsel for NEXTLINK Communications Companies

DISTRICT OF COLUMBIA)
)
)

VERIFICATION

R. Gerard Salemme, being first duly sworn under oath, states that he is Senior Vice President, External Affairs and Industry Relations of NEXTLINK Long Distance Services, Inc., that he has read the foregoing Application and that the matters stated therein are true to the best of his knowledge and belief.

R. Gerard Salemme

SUBSCRIBED and SWORN
to before me this 30th day
of July, 1999.

Notary Public, Marla J. Davis
Washington, DC

My Commission Expires October 31, 2002

CERTIFICATE OF INCORPORATION

OF

NEW NEXTLINK COMMUNICATIONS, INC.

Pursuant to § 102 of the General Corporation Law of Delaware, the undersigned does hereby submit this Certificate of Incorporation for the purpose of forming a business corporation.

1. Name. The name of the corporation is:

NEW NEXTLINK COMMUNICATIONS, INC.

New NEXTLINK Communications, Inc., is referred to as the "Corporation" hereafter in this Certificate of Incorporation.

2. Purpose. The nature of the business or purpose to be conducted or promoted by the Corporation is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of Delaware.

3. Shares. The Corporation shall have authority to issue One Hundred Fifty-Four Million Four Hundred Sixty-Seven Thousand Six Hundred (154,467,600) shares of common stock (the "Common Stock"), which shall be divided into two classes, One Hundred Ten Million Three Hundred Thirty-Four Thousand (110,334,000) shares of Class A Common Stock, par value $0.02 per share (the "Class A Common Stock"), and Forty-Four Million One Hundred Thirty-Three Thousand Six Hundred (44,133,600) shares of Class B Common Stock, par value $0.02 per share (the "Class B Common Stock"). The Corporation shall have authority to issue Twenty-Five Million (25,000,000) shares of preferred stock, par value $.01 per share (the "Preferred Stock").

The Class A and Class B Common Stock are entitled to vote on all matters which come before the stockholders. Subject to the differential voting power hereafter described in this paragraph 3, all Common Stock shall vote together as a single class. Each share of Class A Common Stock shall have one (1) vote and each share of Class B Common Stock shall have ten (10) votes on all matters on which holders of Common Stock are entitled to vote. Each share of Class B Common Stock may be converted, at any time and at the option of the holder, into one share of Class A Common Stock. Each share of Class B Common Stock may also be converted, at the option of the Corporation as determined in the sole discretion of its Board of Directors, into one share of Class A Common Stock at any time such Class B Common Stock is

STATE OF DELAWARE
SECRETARY OF STATE
DIVISION OF CORPORATIONS
FILED 09:00 AM 05/18/1998
981190547 – 2898326

transferred, or is presented to the Company for transfer on the Company's records by the holder of such Class B Common Stock, whether such transfer results from a contractual obligation of the holder, by operation of law, by a change in control of the holder, by testamentary disposition or gift, or for any other reason.

Except with regard to the differential voting power hereinbefore described in this paragraph 3, the Class A Common Stock and the Class B Common Stock shall carry identical characteristics, rights, preferences, and limitations, including but not limited to participating equally in any dividends when and as declared by the Directors out of funds lawfully available therefor and in any distribution resulting from a liquidation or distribution of assets, whether voluntary or involuntary, in each case subject to any preferential rights granted to any series of Preferred Stock that may be then outstanding.

Shares of Preferred Stock of the Corporation may be issued from time to time in one or more classes or series, each of which class or series shall have such distinctive designation or title as shall be fixed by the Board of Directors of the Corporation (the "Board of Directors") and recorded in a Certificate of Designations adopted and filed as required by § 151 of the General Corporation Law of Delaware prior to the issuance of any shares thereof. Each such class or series of Preferred Stock shall have such voting powers, full or limited, or no voting powers, and such preferences and relative participating, option or other special rights and such qualifications, limitations or restrictions thereof, as shall be stated in such resolution or resolutions providing for the issue of such class or series of Preferred Stock as may be adopted from time to time by the Board of Directors prior to the issuance of any shares thereof pursuant to the authority hereby expressly vested in it, all in accordance with the laws of the State of Delaware.

4. **Bylaws.** In furtherance and not in limitation of the powers conferred by statute, the bylaws of the Corporation may be made, altered, amended or repealed by the stockholders or by a majority of the entire Board of Directors.

5. **Registered Agent and Office.** The name of the initial registered agent of this corporation and the address of its initial registered office are as follows:

Name	Address
The Corporation Trust Company	1209 Orange Street Wilmington, DE 19801 New Castle County

8. **Directors.** The number of directors of this corporation shall be determined in the manner specified by the Bylaws and may be increased or decreased from time to time in the manner provided therein. The initial Board of Directors shall consist of one director and his name and address are as follows:

I, EDWARD J. FREEL, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY THE ATTACHED IS A TRUE AND CORRECT COPY OF THE CERTIFICATE OF INCORPORATION OF "NEW NEXTLINK COMMUNICATIONS, INC.", FILED IN THIS OFFICE ON THE EIGHTEENTH DAY OF MAY, A.D. 1998, AT 9 O'CLOCK A.M.

1793 • 1847 • 1907

Edward J. Freel

Edward J. Freel, Secretary of State

2898326 8100

981215125

AUTHENTICATION: 9119870

DATE: 06-04-98

Name	Address
R. Bruce Easter, Jr.	**NEXTLINK Communications, Inc.** **155 108th Avenue NE** **Ste. 810** **Bellevue, WA 98004**

The term of the initial directors shall be until the first annual meeting of the stockholders or until their successors are elected and qualified, unless removed in accordance with the provisions of the Bylaws. Elections of directors need not be by written ballot.

9. **Incorporator.** The name and mailing address of the incorporator are as follows:

Greg F. Adams
Davis Wright Tremaine
2600 Century Square
1501 Fourth Avenue
Seattle, WA 98101-1688

10. **Indemnification.**

(a) The Corporation shall indemnify to the fullest extent permitted under and in accordance with the laws of the State of Delaware any person who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative by reason of the fact that he or she is or was a director, officer, employee or agent of the Corporation, or is or was serving at the request of the Corporation as a director, officer, trustee, employee or agent of or in any other capacity with another corporation, partnership, joint venture, trust or other enterprise, against expenses (including attorneys' fees and costs), judgments, fines and amounts paid in settlement actually and reasonably incurred by him or her in connection with such action, suit or proceeding if he or she acted in good faith and in a manner he or she reasonably believed to be in or not opposed to the best interests of the Corporation, and, with respect to any criminal action or proceeding, had no reasonable cause to believe his conduct was unlawful.

(b) Expenses incurred in defending a civil or criminal action, suit or proceeding shall (in the case of any action, suit or proceeding against a director of the Corporation) or may (in the case of any action, suit or proceeding against an officer, trustee, employee or agent) be paid by the Corporation in advance of the final disposition of such action, suit or proceeding as authorized by the Board of Directors upon receipt of an undertaking by or on behalf of the indemnified person to repay such amount if it shall ultimately be determined that he or she is not entitled to be indemnified by the Corporation as authorized in this paragraph 10.

(c) The indemnification and other rights set forth in this paragraph 10 shall not be exclusive of any provisions with respect thereto in the bylaws or any other contract or agreement between the Corporation and any officer, director, employee or agent of the Corporation.

(d) Neither the amendment nor repeal of this paragraph 10, subparagraph (a), (b) or (c), nor the adoption of any provision of this Certificate of Incorporation inconsistent with this paragraph 10, subparagraph (a), (b) or (c), shall eliminate or reduce the effect of this paragraph 10, subparagraphs (a), (b) and (c), in respect of any matter occurring before such amendment, repeal or adoption of an inconsistent provision or in respect of any cause of action, suit or claim relating to any such matter which would have given rise to a right of indemnification or right to receive expenses pursuant to this paragraph 10, subparagraph (a), (b) or (c), if such provision had not been so amended or repealed or if a provision inconsistent therewith had not been so adopted.

11. **Limitation of Director Liability.** A director shall have no liability to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, except for any breach of the director's duty of loyalty to the corporation or its stockholders, acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law by the director, conduct violating § 174 of the General Corporation Law of Delaware, or for any transaction from which the director will personally receive a benefit in money, property or services to which the director is not legally entitled. If the General Corporation Law of Delaware is hereafter amended to authorize corporate action further eliminating or limiting the personal liability of directors, then the liability of a director shall be eliminated or limited to the full extent permitted by the General Corporation Law of Delaware, as so amended. Any repeal or modification of this Article shall not adversely affect any right or protection of a director of the corporation existing at the time of such repeal or modification for or with respect to an act or omission of such director occurring prior to such repeal or modification.

THE UNDERSIGNED, being the incorporator hereinbefore named, for the purpose of forming a Corporation pursuant to the General Corporation Law of Delaware, executes this Certificate, hereby declaring and certifying that this is his act and deed and the facts herein stated are true and, accordingly, has hereunto set his hand this 18th day of May, 1998.

Greg F. Adams
Incorporator

Exh. B

Lci 935 809

FEB 2 6 1999

ARTICLES OF INCORPORATION

OF

NEXTLINK LONG DISTANCE SERVICES, INC.

Pursuant to RCW 23B.02.020 of the Washington Business Corporation Act, the undersigned does hereby submit these Articles of Incorporation for the purpose of forming a business corporation.

ARTICLE I

NAME

The name of this corporation is NEXTLINK LONG DISTANCE SERVICES, INC.

ARTICLE II

PURPOSES

This corporation is organized for the following purposes:

To engage in any business, trade or activity that may be conducted lawfully by a corporation organized under the Washington Business Corporation Act.

ARTICLE III

SHARES

This corporation is authorized to issue one thousand (1,000) shares of common stock with no par value.

ARTICLE IV

PREEMPTIVE RIGHTS

Each Shareholder shall have preemptive rights to acquire additional shares which may be issued by this corporation to the extent preemptive rights apply to such shares under the Washington Business Corporation Act.

ARTICLE V

NO CUMULATIVE VOTING

At each election for directors, every shareholder entitled to vote at such election has the right to vote in person or by proxy the number of shares held by such shareholder for as many persons as there are directors to be elected. No cumulative voting for directors shall be permitted.

ARTICLE VI

BYLAWS

The Board of Directors shall have the power to adopt, amend or repeal the Bylaws or adopt new Bylaws. Nothing herein shall deny the concurrent power of the shareholders to adopt, alter, amend or repeal the Bylaws.

ARTICLE VII

REGISTERED AGENT AND OFFICE

The name of the initial registered agent of this corporation and the address of its initial registered office are as follows:

Registered Agent	Office
DWTR&J Corp.	2600 Century Square 1501 Fourth Avenue Seattle, WA 98101-1688

ARTICLE VIII

DIRECTORS

A. The number of directors of this corporation shall be determined in the manner specified by the Bylaws and may be increased or decreased from time to time in the manner provided therein.

B. The term of the initial directors shall be until the first annual meeting of the shareholders or until their successors are elected and qualified, unless removed in accordance with the provisions of the Bylaws.

ARTICLE IX

SHAREHOLDER VOTING REQUIREMENTS FOR CERTAIN TRANSACTIONS

In order to obtain shareholder approval in connection with the following corporate actions, such actions must be approved by each voting group of shareholders entitled to vote thereon by a majority of all the votes entitled to be cast by that voting group: amendment of the Articles of Incorporation; a plan of merger or share exchange; the sale, lease, exchange, or other disposition of all, or substantially all, of the corporation's assets other than in the usual and regular course of business; or dissolution of the corporation.

ARTICLE X

INCORPORATOR

The name and address of the incorporator are as follows:

Name	Address
Jeff Belfiglio	1800 Bellevue Place 10500 N.E. 8th Street Bellevue, Washington 98004

ARTICLE XI

LIMITATION OF DIRECTORS' LIABILITY

A director shall have no liability to the corporation or its shareholders for monetary damages for conduct as a director, except for acts or omissions that involve intentional misconduct by the director, or a knowing violation of law by the director, or for conduct violating RCW 23B.08.310, or for any transaction from which the director will personally receive a benefit in money, property or services to which the director is not legally entitled. If the Washington Business Corporation Act is hereafter amended to authorize corporate action further eliminating or limiting the personal liability of directors, then the liability of a director shall be eliminated or limited to the full extent permitted by the Washington Business Corporation Act, as so amended. Any repeal or modification of this Article shall not adversely affect any right or protection of a director of the corporation existing at the time of such repeal or modification for or with respect to an act or omission of such director occurring prior to such repeal or modification.

ARTICLE XII

INDEMNIFICATION OF DIRECTORS AND OFFICERS

Section 1. Right to Indemnification. Each person who was, or is threatened to be made a party to or is otherwise involved (including, without limitation, as a witness) in any actual or threatened action, suit or proceeding, whether civil, criminal, administrative or investigative, by reason of the fact that he or she is or was a director or officer of the corporation or, while a director or officer, he or she is or was serving at the request of the corporation as a director, trustee, officer, employee or agent of another corporation or of a partnership, joint venture, trust or other enterprise, including service with respect to employee benefit plans, whether the basis of such proceeding is alleged action in an official capacity as a director, trustee, officer, employee or agent or in any other capacity while serving as a director, trustee, officer, employee or agent, shall be indemnified and held harmless by the corporation, to the full extent permitted by applicable law as then in effect, against all expense, liability and loss (including attorney's fees, judgments, fines, ERISA excise taxes or penalties and amounts to be paid in settlement) actually and reasonably incurred or suffered by such person in connection therewith, and such indemnification shall continue as to a person who has ceased to be a director, trustee, officer, employee or agent and shall inure to the benefit of his or her heirs, executors and administrators; provided, however, that except as provided in Section 2 of this Article with respect to proceedings seeking to enforce rights to indemnification, the corporation shall indemnify any such person seeking indemnification in connection with a proceeding (or part thereof) initiated by such person only if such proceeding (or part thereof) was authorized by the board of directors of the corporation. The right to indemnification conferred in this Section 1 shall be a contract right and shall include the right to be paid by the corporation the expenses incurred in defending any such proceeding in advance of its final disposition; provided, however, that the payment of such expenses in advance of the final disposition of a proceeding shall be made only upon delivery to the corporation of an undertaking, by or on behalf of such director or officer, to repay all amounts so advanced if it shall ultimately be determined that such director or officer is not entitled to be indemnified under this Section 1 or otherwise.

Section 2. Right of Claimant to Bring Suit. If a claim under Section 1 of this Article is not paid in full by the corporation within sixty (60) days after a written claim has been received by the corporation, except in the case of a claim for expenses incurred in defending a proceeding in advance of its final disposition, in which case the applicable period shall be twenty (20) days, the claimant may at any time thereafter bring suit against the corporation to recover the unpaid amount of the claim and, to the extent successful in whole or in part, the claimant shall be entitled to be paid also the expense of prosecuting such claim. The claimant shall be presumed to be entitled to indemnification under this Article upon submission of a written claim (and, in an action brought to enforce a claim for expenses incurred in defending any proceeding in advance of its final disposition, where the required undertaking has been tendered to the corporation), and thereafter the corporation shall have the burden of proof to overcome the presumption that the claimant is not so entitled. Neither the failure of the corporation (including its board of directors, independent legal counsel or its shareholders) to have made a determination prior to the commencement of such action that indemnification of or reimbursement or advancement of expenses to the claimant is proper in the circumstances nor an actual determination by the corporation (including its board of directors, independent legal counsel or its shareholders) that the claimant is not entitled to indemnification or to the reimbursement or advancement of expenses shall be a defense to the action or create a presumption that the claimant is not so entitled.

Section 3. Nonexclusivity of Rights. The right to indemnification and the payment of expenses incurred in defending a proceeding in advance of its final disposition conferred in this Article shall not be exclusive of any other right which any person may have or hereafter acquire under any statute, provision of the Articles of Incorporation, Bylaws, agreement, vote of shareholders or disinterested directors or otherwise.

Section 4. Insurance, Contracts and Funding. The corporation may maintain insurance, at its expense, to protect itself and any director, trustee, officer, employee or agent of the corporation or another corporation, partnership, joint venture, trust or other enterprise against any expense, liability or loss, whether or not the corporation would have the power to indemnify such person against such expense, liability or loss under the Washington Business Corporation Act. The corporation may, without further shareholder action, enter into contracts with any director or officer of the corporation in furtherance of the provisions of this Article and may create a trust fund, grant a security interest or use other means (including, without limitation, a letter of credit) to ensure the payment of such amounts as may be necessary to effect indemnification as provided in this Article.

Section 5. Indemnification of Employees and Agents of the Corporation. The corporation may, by action of its board of directors from time to time, provide indemnification and pay expenses in advance of the final disposition of a proceeding to employees and agents of the corporation with the same scope and effect as the provisions of this Article with respect to the indemnification and advancement of expenses of directors and officers of the corporation or pursuant to rights granted pursuant to, or provided by, the Washington Business Corporation Act or otherwise.

ARTICLE XIII

EFFECTIVE DATE

These Articles of Incorporation shall be effective upon filing.

DATED this 25th day of February, 1999.

Jeff Belfiglio

JEFF BELFIGLIO, Incorporator

CONSENT TO SERVE AS REGISTERED AGENT

DWTR&J Corp., a Washington corporation, hereby consents to serve as Registered Agent, in the State of Washington, for NEXTLINK LONG DISTANCE SERVICES, INC. DWTR&J Corp. understands that as agent for said corporation, it will be responsible to receive service of process in the name of said corporation; to forward all mail to said corporation; and to immediately notify the office of the Secretary of State in the event of its resignation, or of any changes in the registered office address of 2600 Century Square, 1501 Fourth Avenue, Seattle, WA 98101-1688.

DATED this 25th day of February, 1999.

DWTR&J CORP., a Washington corporation

Sharon Lawrence

SHARON LAWRENCE, Vice President

2600 Century Square
1501 Fourth Avenue
Seattle, Washington 98101-1688

STATE of WASHINGTON

SECRETARY of STATE

I, RALPH MUNRO, Secretary of State of the State of Washington and custodian of its seal, hereby issue this

CERTIFICATE OF INCORPORATION

to

NEXTLINK LONG DISTANCE SERVICES, INC.

a Washington Profit corporation. Articles of Incorporation were filed for record in this office on the date indicated below.

UBI Number: 601 935 809

Date: February 26, 1999

Given under my hand and the Seal of the State of Washington at Olympia, the State Capital

Ralph Munro, Secretary of State

2-603100-5

FLORIDA DEPARTMENT OF STATE
Katherine Harris
Secretary of State

June 21, 1999

CSC

,

Qualification documents for NEXTLINK LONG DISTANCE SERVICES, INC. were filed on June 21, 1999 and assigned document number F99000003166. Please refer to this number whenever corresponding with this office.

Your corporation is now qualified and authorized to transact business in Florida as of the file date.

A corporation annual report will be due this office between January 1 and May 1 of the year following the calendar year of the file date. A Federal Employer Identification (FEI) number will be required before this report can be filed. If you do not already have an FEI number, please apply NOW with the Internal Revenue by calling 1-800-829-3676 and requesting form SS-4.

Please be aware if the corporate address changes, it is the responsibility of the corporation to notify this office.

Should you have any questions regarding this matter, please telephone (850) 487-6091, the Foreign Qualification/Tax Lien Section.

Agnes Lunt
Document Specialist
Division of Corporations

Letter Number: 199A00032903

Account number: 072100000032

Account charged: 70.00

APPLICATION BY FOREIGN CORPORATION FOR AUTHORIZATION TO TRANSACT BUSINESS IN FLORIDA

IN COMPLIANCE WITH SECTION 607.1503, FLORIDA STATUTES, THE FOLLOWING IS SUBMITTED TO REGISTER A FOREIGN CORPORATION TO TRANSACT BUSINESS IN THE STATE OF FLORIDA:

1. NEXTLINK Long Distance Services, Inc.
(Name of corporation: must include the word "INCORPORATED", "COMPANY", "CORPORATION" or words or abbreviations of like import in language as will clearly indicate that it is a corporation instead of a natural person or partnership if not so contained in the name at present.)

2. Washington
(State or country under the law of which it is incorporated)

3. 91-1957034
(FEI number, if applicable)

4. February 26, 1999
(Date of Incorporation)

5. Perpetual
(Duration: Year corp. will cease to exist or "perpetual")

6. Upon Qualification
(Date first transacted business in Florida. (SEE SECTIONS 607.1501, 607.1502, AND 817.155, F.S.)

7. Suite 2200, 500 - 108th Avenue N.E.
Bellevue, WA 98004
(Current mailing address)

8. Operating a telecommunications service. To engage in any act or activity for which corporations may be organized.
(Purpose(s) of corporation authorized in home state or country to be carried out in the state of Florida)

9. **Name and street address of Florida registered agent:** (P.O. Box or Mail Drop Box NOT acceptable)

Name: Corporation Service Company

Office Address: 1201 Hays Street

Tallahassee, Florida, 32301
(Zip Code)

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DIVISION OF CORPORATIONS
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10. **Registered agent's acceptance:**

Having been named as registered agent and to accept service of process for the above stated corporation at the place designated in this application, I hereby accept the appointment as registered agent and agree to act in this capacity. I further agree to comply with the provisions of all statutes relative to the proper and complete performance of my duties, and I am familiar with and accept the obligations of my position as registered agent.

Corporation Service Company

By: [signature]
(Registered agent's signature)

11. Attached is a certificate of existence duly authenticated, not more than 90 days prior to delivery of this application to the Department of State, by the Secretary of State or other official having custody of corporate records in the jurisdiction under the law of which it is incorporated.

12. Names and addresses of officers and/or directors: (Street address **ONLY** - P. O. Box **NOT** acceptable)

A. DIRECTORS (Street address only- P. O . Box NOT acceptable)

Chairman: See attached officers/directors rider

Address: ______

Vice Chairman: ______

Address: ______

Director: ______

Address: ______

Director: ______

Address: ______

B. OFFICERS (Street address only- P. O. Box NOT acceptable)

President: See attached officers/directors rider

Address: ______

Vice President: ______

Address: ______

Secretary: ______

Address: ______

Treasurer: ______

Address: ______

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NOTE: If necessary, you may attach an addendum to the application listing additional officers and/or directors.

13. Jay D. Hull
(Signature of Chairman, Vice Chairman, or any officer listed in number 12 of the application)

14. Jay D. Hull, Assistant Secretary
(Typed or printed name and capacity of person signing application)

NEXTLINK LONG DISTANCE SERVICES, INC.

OFFICERS/DIRECTORS RIDER

The address for each of the following directors and officers is:

500 - 108th Avenue N.E.
Suite 2200
Bellevue, WA 98004

Directors:

George M. Tronsrue III

R. Bruce Easter, Jr.

Kathleen Iskra

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DIVISION OF CORPORATIONS
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Officers:

George M. Tronsrue III	CEO, COO, President
Charles P. Daniels	Vice President
Jan Loichle	Vice President
R. Bruce Easter, Jr.	Vice President, Secretary, General Counsel
Kathleen Iskra	Vice President, CFO, Treasurer
R. Gerard Salemme	Senior Vice President
Michael McHale	Vice President
Jay D. Hull	Assistant Secretary
Richard A. Montfort, Jr.	Assistant Secretary

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Exh. C

BIOGRAPHIES OF NEXTLINK OFFICERS

George M. Tronsrue III
President and Chief Operating Officer

Mr. Tronsrue has been President of NEXTLINK Communications, Inc., since July 1998 and Chief Operating Officer of NEXTLINK since October 1997. Prior to that, Mr. Tronsrue was part of the initial management team of ACSI from February 1994 to September 1997, and was responsible for planning and overseeing the operations of ACSI for its first three years serving as Chief Operating Officer, President, Strategy and Technology Development Division and Executive Vice President, Planning and Development. Prior to that, Mr. Tronsrue served as the Regional Vice President of the Central Region of Teleport Communications Group ("TCG"), and as Vice President, Emerging Markets overseeing the start-up of TCG's initial eight cable television partnerships. Before TCG, Mr. Tronsrue was at MFS Communications from its inception in 1987 until 1992. At MFS, Mr. Tronsrue served as Vice President, Corporate Planning and Information Management; Vice President, Field Sales; Vice President and General Manager for MFS New York during its first year of operations and Executive Vice President, MFS Internet. Prior to MFS, Mr. Tronsrue served at MCI from 1983 to 1986 in a variety of engineering and operations roles, culminating as Director of Operations, Michigan and Ohio.

R. Gerard Salemme
Senior Vice President, External Affairs and Industry Relations

Mr. Salemme has been Senior Vice President, External Affairs and Industry Relations of NEXTLINK since July 1997. Prior to joining NEXTLINK, Mr. Salemme was Vice President, Government Affairs at AT&T Corporation from December 1994. Prior to joining AT&T, Mr. Salemme was Senior Vice President, External Affairs at McCaw Cellular from 1991 to December 1994.

Charles P. Daniels
Vice President & Chief Technology Officer

Mr. Daniels has been Vice President, Chief Technology Officer of NEXTLINK since July 1997. Prior to that, Mr. Daniels was Vice President, Chief Marketing officer of NEXTLINK from November 1995. From 1992 to 1995, Mr. Daniels worked for MCI where he was the founder and Program Manager of the network MCI Developers Lab. Mr. Daniels was also a founding member of MCI's Advanced Technology Group. Prior to joining MCI, Mr. Daniels worked for Manufacturers Hanover Trust from 1989 to 1992 as Vice President, Strategic Technology & Research, where he was responsible for evaluating and implementing new technologies that either reduced costs or generated new revenue.

R. Bruce Easter, Jr.
Vice President, General Counsel & Secretary

Mr. Easter has been Vice President, General Counsel and Secretary of NEXTLINK since January 1995. From 1986 to December 1994, he was an associate and then partner in the law firm of Davis Wright Tremaine in Seattle, Washington, where he focused on communications law and media matters.

Kathleen H. Iskra
Vice President, Chief Financial Officer and Treasurer

Ms. Iskra has been Vice President and Chief Financial Officer and Treasurer of NEXTLINK since January 1996. Prior to that, she was President and Chief Executive Officer of Horizon Air, a wholly-owned subsidiary of Alaska Air Group. Prior to her appointment at Horizon Air, Ms. Iskra served as staff Vice President of Finance and Controller of Alaska Airlines and Alaska Air Group. Ms. Iskra's service with Alaska began in 1987, when she was appointed Controller. Prior to joining Alaska, she was an audit manager with Arthur Andersen.

Janice E. Loichle
Vice President, Chief of Local Exchange Operations

NEXTLINK since October 1996. Prior to that, Ms. Loichle was President of NEXTLINK Solutions (an enhanced services subsidiary) from July 1995. Prior to joining NEXTLINK, Ms. Loichle was Executive Vice President at U.S. Signal in Detroit and Grand Rapids, Michigan from April 1993 to July 1995. At U.S. Signal, Ms. Loichle was responsible for Finance, Systems, Administration and was also involved in the initial CLEC development in Grand Rapids. From 1990 to 1993, Ms. Loichle was Assistant Vice President of Finance for SP Telecom in San Francisco. Prior to that, Ms. Loichle was Vice President of Financial Operations for Lexitel/Allnet/ALC in Birmingham, Michigan from December 1980 to October 1989.

Michael J. McHale, Jr.
Chief Marketing Officer

Mr. McHale has been Vice President, Chief Marketing Officer of NEXTLINK since November 1997. Prior to joining NEXTLINK, Mr. McHale served as Vice President and General Manager of the Phoenix market and Regional Vice President at Teleport Communications Group, Inc. from 1993, developing the Phoenix market from its inception. Prior to that, from 1991 to 1993, he was Vice President, Product Marketing and Development at MFS Intelenet, Inc. and was responsible for planning and implementing MFS's initial introduction of switched services in New York City.

Richard A. Montfort, Jr.
Assistant Secretary

Mr. Montfort has been Assistant Secretary of NEXTLINK since July 1998. From October 1992 to February 1998, he was associated with the law firm of Preston Gates & Ellis in Seattle, Washington, where he focused on securities law and mergers and acquisitions.

Jay D. Hull
Assistant General Counsel and Assistant Secretary

Mr. Hull has been Assistant Secretary of NEXTLINK since August 1998. Mr. Hull began practicing law in 1984 and become a partner at Davis Wright Tremaine in Portland, Oregon in 1991. He represented NEXTLINK at Davis Wright Tremaine from the time NEXTLINK was formed in 1994.

Exh. D

As Filed with the Securities and Exchange Commission on November 16, 1998

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 1998

Commission file number: 000-22939

NEXTLINK Communications, Inc.
NEXTLINK Capital, Inc.
(Exact name of registrant as specified in its charter)

Delaware Washington	91-1738221 91-1716062
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
500 108th Avenue NE, Suite 2200, Bellevue, WA	98004
(Address of principal executive offices)	(Zip Code)

(425) 519-8900
(Registrant's telephone number, including area code)

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

As of November 1, 1998, the number of shares of Class A and Class B common stock of NEXTLINK Communications, Inc. issued and outstanding was 21,232,980 and 31,133,502, respectively, and there were 1,000 shares of common stock of NEXTLINK Capital, Inc., all of which 1,000 shares were held by NEXTLINK Communications, Inc.

NEXTLINK Capital, Inc. meets the conditions set forth in General Instruction H(1)(a) and (b) of Form 10-Q and is therefore filing this Form with the reduced disclosure format.

PART I. FINANCIAL INFORMATION

Item 1(a). Financial Statements

NEXTLINK Communications, Inc.
Consolidated Balance Sheets
(Dollars in thousands, except per share amounts)
(Amounts as of September 30, 1998 are unaudited)

	September 30, 1998	December 31, 1997
ASSETS		
Current assets:		
Cash and cash equivalents	$ 392,350	$ 389,074
Marketable securities	784,493	353,283
Accounts receivable, net	29,525	22,955
Other	12,273	4,530
Pledged securities	42,992	41,425
Total current assets	1,261,633	811,267
Pledged securities	–	21,185
Property and equipment, net	448,550	253,653
Goodwill, net	55,813	52,278
Other assets, net	260,182	78,770
Total assets	$ 2,026,178	$ 1,217,153
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Accounts payable	$ 24,634	$ 26,776
Accrued expenses	32,119	13,082
Accrued interest payable	40,615	18,880
Notes payable and current portion of capital lease obligations	4,021	10,844
Total current liabilities	101,389	69,582
Long-term debt	1,503,263	750,000
Capital lease obligations and other long-term liabilities	16,096	10,842
Total liabilities	1,620,748	830,424
Commitments and contingencies		
Redeemable preferred stock, par value $0.01 per share, 25,000,000 shares authorized; 14% Preferred, aggregate liquidation preference $358,646, 7,009,348 and 6,322,031 shares issued and outstanding in 1998 and 1997, respectively; 6 ½% Convertible Preferred, 4,000,000 and 0 shares issued and outstanding in 1998 and 1997, respectively	543,258	313,319
Common stock subject to redemption, par value $0.02 per share, 519,950 Class B shares issued and outstanding in 1997	–	4,950
Shareholders' equity (deficit):		
Common Stock, par value $0.02 per share, stated at amounts paid in; Class A, 110,334,000 shares authorized, 20,830,169 and 19,167,899 shares issued and outstanding in 1998 and 1997, respectively; Class B, 44,133,600 shares authorized, 33,133,502 and 33,746,573 shares issued and outstanding in 1998 and 1997, respectively	352,018	330,561
Deferred compensation	(12,894)	(9,596)
Accumulated deficit	(476,952)	(252,505)
Total shareholders' equity (deficit)	(137,828)	68,460
Total liabilities and shareholders' equity (deficit)	$ 2,026,178	$ 1,217,153

See accompanying notes to unaudited interim consolidated financial statements.

Consolidated Statements of Operations
(Dollars in thousands, except per share amounts)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	1998	1997	1998	1997
Revenue	$ 37,817	$ 13,390	$ 96,392	$ 35,058
Costs and expenses:				
Operating	32,828	13,916	85,448	35,857
Selling, general and administrative	41,565	19,318	109,599	48,421
Deferred compensation	1,720	334	3,104	1,449
Depreciation	11,334	3,898	26,243	9,952
Amortization	3,444	1,631	10,898	4,508
Total costs and expenses	90,891	39,097	235,292	100,187
Loss from operations	(53,074)	(25,707)	(138,900)	(65,129)
Interest income	21,559	4,868	56,116	15,560
Interest expense	(37,434)	(10,746)	(99,050)	(32,787)
Net loss	$ (68,949)	$ (31,585)	$ (181,834)	$ (82,356)
Preferred stock dividends and accretion of preferred stock redemption obligation, including issue costs	(15,734)	(10,798)	(42,613)	(28,151)
Net loss applicable to common shares	$ (84,683)	$ (42,383)	$ (224,447)	$ (110,507)
Net loss per share	$ (1.57)	$ (1.08)	$ (4.18)	$ (2.87)
Shares used in computation of net loss per share	53,883,632	39,257,126	53,658,325	38,536,851

See accompanying notes to unaudited interim consolidated financial statements.

NEXTLINK Communications, Inc.
Consolidated Statements of Cash Flows
(Dollars in thousands)
(Unaudited)

	Nine Months Ended September 30, 1998	1997
OPERATING ACTIVITIES:		
Net loss	$ (181,834)	$ (82,356)
Adjustments to reconcile net loss to net cash used in operating activities:		
Deferred compensation expense	3,104	1,449
Equity in loss of affiliates	2,635	1,688
Depreciation and amortization	37,141	14,460
Accretion of interest on senior notes	18,940	–
Changes in assets and liabilities, net of effects from acquisitions:		
Accounts receivable	(6,570)	(3,062)
Other assets	(10,588)	(662)
Accounts payable	(8,016)	(6,328)
Accrued expenses and other liabilities	18,683	5,370
Accrued interest payable	21,735	10,208
Net cash used in operating activities	(104,770)	(59,233)
INVESTING ACTIVITIES:		
Purchase of property and equipment	(209,136)	(89,146)
Net assets acquired in business and asset acquisitions (net of cash acquired)	–	(41,239)
Cash withdrawn from escrow to be used in business acquisition	–	6,000
Assets acquired in network lease agreement	(92,000)	–
Contribution to NEXTBAND for purchase of spectrum licenses	(67,354)	–
Investments in unconsolidated affiliates	(13,337)	(6,342)
Maturity of pledged securities	19,636	18,049
Purchase of marketable securities	(3,347,468)	(28,812)
Sale of marketable securities	2,916,258	–
Net cash used in investing activities	(793,401)	(141,490)

– Continued –

NEXTLINK Communications, Inc.
Consolidated Statements of Cash Flows (Cont'd)
(Dollars in thousands)
(Unaudited)

	Nine Months Ended September 30, 1998	Nine Months Ended September 30, 1997
FINANCING ACTIVITIES:		
Net proceeds from issuance of redeemable preferred stock	$ 193,824	$ 274,000
Repayment of note payable and capital lease obligations	(7,346)	(1,380)
Repayment of payable to affiliates	–	(1,500)
Proceeds from issuance of common stock upon exercise of stock options	2,021	111
Dividends paid on convertible preferred stock	(6,500)	–
Repayment (issuance) of loans to related parties	2,357	(2,825)
Proceeds from issuance of senior notes (net of discount)	734,323	–
Costs incurred in connection with financing	(17,232)	(402)
Net cash provided by financing activities	901,447	268,004
Net increase in cash and cash equivalents	3,276	67,281
Cash and cash equivalents, beginning of period	389,074	76,807
Cash and cash equivalents, end of period	$ 392,350	$ 144,088
SUPPLEMENTAL CASH FLOW DISCLOSURES:		
Noncash financing and investing activities:		
Redeemable preferred stock dividends, paid in redeemable preferred shares	$ 34,366	$ 20,413
Accrued redeemable preferred stock dividends, payable in redeemable preferred shares, and accretion of preferred stock redemption obligation and issue costs	$ 1,747	$ 7,127
Issuance of Class B common stock for purchase of minority interests	$ 5,727	$ –
Capital lease obligations assumed	$ 5,065	$ 4,725
Class A common stock issued under lease arrangement	$ –	$ 1,400
Cash paid for interest	$ 58,860	$ 22,579

See accompanying notes to unaudited interim consolidated financial statements.

NEXTLINK Communications, Inc.
Notes to Interim Consolidated Financial Statements
(Unaudited)

1. Basis of Presentation

The consolidated financial statements include the accounts of NEXTLINK Communications, Inc., a Delaware corporation, and its majority-owned subsidiaries (collectively referred to as the Company). The Company, through predecessor entities, was formed on September 16, 1994 and, through its subsidiaries, provides competitive local telecommunications services in selected markets in the United States. The Company is a majority-owned subsidiary of Eagle River Investments, L.L.C. (Eagle River).

The Company's financial statements include 100% of the assets, liabilities and results of operations of subsidiaries in which the Company has a controlling interest of greater than 50%. The Company's investment in Telecommunications of Nevada, L.L.C. (Nevada L.L.C.), a limited liability company in which the Company has a 40% interest and which operates a network that is managed by the Company in Las Vegas, Nevada, is accounted for on the equity method. All operational statistics of the Company included in this Report include 100% of the operational statistics of Nevada L.L.C. Investments in entities in which the Company has voting interests of not more than 20% are accounted for on the cost method. All significant intercompany accounts and transactions have been eliminated.

The interim financial statements are unaudited and have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Form 10-KSB as filed with the Securities and Exchange Commission on March 25, 1998.

The financial information included herein reflects all adjustments (consisting only of normal recurring adjustments) which are, in the opinion of management, necessary to a fair presentation of the results for interim periods. The results of operations for the three and nine-month periods ended September 30, 1998 are not necessarily indicative of the results to be expected for the full year.

2. Financings

Debt

On March 3, 1998, the Company completed the sale of $335.0 million in aggregate principal amount of 9% Senior Notes due March 15, 2008 (9% Senior Notes). Proceeds from the sale net of discounts, underwriting commissions, advisory fees and expenses totaled approximately $326.5 million. Interest payments on the 9% Senior Notes are due semi-annually. The 9% Senior Notes are redeemable at the option of the Company, in whole or in part, beginning March 15, 2003.

On April 1, 1998, the Company completed the sale of 9.45% Senior Discount Notes (9.45% Notes), due April 15, 2008. The 9.45% Notes were issued at a discount from their principal amount to generate aggregate gross proceeds to the Company of approximately $400.0 million. Proceeds net of underwriting commissions, advisory fees and expenses totaled $390.9 million. The 9.45% Notes accrete at a rate of 9.45% compounded semi-annually, to an aggregate principal amount of approximately $637.0 million by April 15, 2003. No cash interest will accrue on the 9.45% Notes until April 15, 2003. Interest will become payable in cash semi-annually beginning on October 15, 2003. The 9.45% Notes are redeemable at the option of the Company, in whole or in part, at any time after April 15, 2003.

The indentures pursuant to which the 9% Senior Notes and the 9.45% Notes (the Notes) are issued contain certain covenants that, among other things, limit the ability of the Company and its subsidiaries to incur additional indebtedness, issue stock in subsidiaries, pay dividends or make other distributions, repurchase equity interests or subordinated indebtedness, engage in sale and leaseback transactions, create certain liens, enter into certain transactions with affiliates, sell assets of the Company and its subsidiaries, and enter into certain mergers and consolidations.

In the event of a change in control or asset disposition of the Company as defined in the indentures, holders of the Notes will have the right to require the Company to purchase their Notes, in whole or in part, at a price equal to 101% of the principal amount thereof, plus accrued and unpaid interest, if any, thereon to the date of purchase. The Notes are senior unsecured obligations of the Company, and are subordinated to all current and future indebtedness of the Company's subsidiaries, including trade payables.

Redeemable Preferred Stock

On March 31, 1998, the Company completed the sale of 4,000,000 shares of 6½% cumulative convertible preferred stock (6½% Preferred Stock) with a liquidation preference of $50 per share. The sale generated gross proceeds to the Company of $200.0 million, and proceeds net of underwriting discounts, advisory fees and expenses of $193.8 million. Each share of 6½% Preferred Stock is convertible, at the option of the holder, into 1.145 shares of the Company's Class A common stock (subject to adjustments in certain circumstances). The Company may cause such conversion rights to expire if the closing price of the Class A common stock exceeds 120% of an implied conversion price (as defined) for 20 days in a 30 consecutive day trading period after April 15, 2001 and through April 15, 2006. Dividends on the 6½% Preferred Stock accrue from March 31, 1998 and are payable in cash quarterly, beginning on June 30, 1998, at an annual rate of 6½% of the liquidation preference thereof. The Company is required to redeem all of the 6½% Preferred Stock outstanding on March 31, 2010 at a redemption price equal to 100% of the liquidation preference thereof, plus accumulated and unpaid dividends to the date of redemption.

3. Network Lease

In February 1998, the Company entered into a 20-year capital lease for exclusive rights to multiple fibers and innerducts throughout New York, New Jersey, Connecticut, Pennsylvania, Delaware, Maryland and Washington D.C. The Company paid $92.0 million in the transaction, of which $80.3 million was placed into escrow pending completion and delivery of segments of the network route to the Company. The payment was recorded as a long-term asset, and will be reclassified as property and equipment as portions of the network are completed. The Company has the option to renew the lease for two additional 10-year terms.

4. Joint Ventures

NEXTBAND

In January 1998, the Company and Nextel Communications, Inc. (Nextel), a nationwide provider of wireless telephone services, formed a joint venture called NEXTBAND Communications, L.L.C. (NEXTBAND), which is owned 50% each by the Company and Nextel. NEXTBAND was the successful bidder in 42 markets covering approximately 105 million POPs, or persons located within the licensed areas owned, in the FCC's local multipoint distribution service (LMDS) auctions, which concluded in March 1998. The Company has contributed $67.4 million to NEXTBAND, representing its pro rata share of NEXTBAND's total bid in the LMDS auctions. The Company is evaluating means to use its access to NEXTBAND's LMDS spectrum to enhance its ability to connect customers to its fiber rings, and to deploy wireless local loop technologies using LMDS frequencies where it determines it cost effective to do so.

INTERNEXT

In July 1998, the Company announced the formation of INTERNEXT L.L.C., which is beneficially owned 50% each by the Company and Eagle River. INTERNEXT has entered into an agreement with Level 3 Communications, LLC (Level 3). Level 3 is constructing a national fiber optic network that is expected to cover more than 16,000 route miles with six or more conduits and connect 50 cities in the United States and Canada. Pursuant to this agreement, INTERNEXT will receive an exclusive interest in 24 fibers in a shared, filled conduit, one entire empty conduit and the right to 25% of the fibers pulled through the sixth and any additional conduits in the network. INTERNEXT will pay $700.0 million in exchange for these rights, the majority of which will be payable as segments of the network are completed and accepted by INTERNEXT, which is expected to occur substantially during 2000 and 2001. The Company has guaranteed 50% of the financial obligations of INTERNEXT under this agreement and, together with Eagle River, has also guaranteed the performance of certain other obligations of INTERNEXT thereunder. The Company anticipates that Nextel will acquire a one-third ownership interest in INTERNEXT, which would reduce the Company's beneficial interest in and obligations with respect to INTERNEXT to one-third.

5. Reclassifications

Certain reclassifications have been made to prior period amounts in order to conform to the current presentation.

6. Subsequent Event

On November 12, 1998, the Company completed the sale of $500.0 million in aggregate principal amount of 10¾% Senior Notes due November 15, 2008 (10¾% Senior Notes). Proceeds from the sale net of underwriting commissions, advisory fees and expenses totaled approximately $488.5 million. Interest payments on the notes are due semi-annually, beginning May 15, 1999. The 10¾% Senior Notes are redeemable at the option of the Company, in whole or in part, beginning November 15, 2003.

The indenture pursuant to which the 10¾% Senior Notes are issued contains certain covenants that, among other things, limit the ability of the Company and its subsidiaries to incur additional indebtedness, issue stock in subsidiaries, pay dividends or make other distributions, repurchase equity interests or subordinated indebtedness, engage in sale and leaseback transactions, create certain liens, enter into certain transactions with affiliates, sell assets of the Company and its subsidiaries, and enter into certain mergers and consolidations. In addition, under the indenture, the Company has agreed to use the net proceeds from the sale for expenditures relating to the construction, improvement and acquisition of new and existing networks and services and direct or indirect investments in certain joint ventures to fund similar expenditures.

In the event of a change in control or asset disposition of the Company as defined in the indentures, holders of the 10¾% Senior Notes will have the right to require the Company to purchase their 10¾% Senior Notes, in whole or in part, at a price equal to 101% of the principal amount thereof, plus accrued and unpaid interest, if any, thereon to the date of purchase. The 10¾% Senior Notes are senior unsecured obligations of the Company, and are subordinated to all current and future indebtedness of the Company's subsidiaries, including trade payables.

PART I. FINANCIAL INFORMATION

Item 1(b). Financial Statements

NEXTLINK Capital, Inc.
Balance Sheets
(Unaudited)

	September 30, 1998	September 30, 1997
ASSETS		
Cash in bank	$ 100	$ 100
SHAREHOLDER'S EQUITY		
Common stock, no par value, 1,000 shares authorized, issued and outstanding	$ 100	$ 100

Notes to Balance Sheets

1. Description

NEXTLINK Capital, Inc. (NEXTLINK Capital) is a Washington corporation and a wholly owned subsidiary of NEXTLINK Communications, Inc. (NEXTLINK). NEXTLINK Capital was formed for the sole purpose of obtaining financing from external sources and is a joint obligor on the 12½% Senior Notes due April 15, 2006 of NEXTLINK. NEXTLINK Capital was initially funded with a $100 contribution from NEXTLINK and has had no operations to date.

2. Basis of Presentation

The interim financial statements have been prepared without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Form 10-KSB as filed with the Securities and Exchange Commission on March 25, 1998.

PART I. FINANCIAL INFORMATION

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

OVERVIEW

Since its inception in 1994, the Company has executed a strategy of constructing and acquiring fiber optic networks and acquiring related telecommunications businesses. Over this period, the Company has pursued this strategy by constructing, acquiring, leasing fibers or capacity on, and entering into agreements to acquire local telecommunications networks.

The Company develops and operates high capacity, local fiber optic networks with broad market coverage in a growing number of markets across the United States. In its switched local service markets, the Company offers its customers a bundled package of local and long distance services and also offers dedicated transmission and competitive access services to long distance carriers and end users. The Company plans to acquire, build or develop networks in new areas, expand its current networks, and also explore the acquisition or licensing of additional enhanced communications services and other telecommunications service providers. These efforts should allow the Company to increase its presence in the marketplace, and facilitate providing a single source solution for the telecommunications needs of its customers.

The Company currently operates 19 facilities-based networks providing switched local and long distance services in 33 markets in 11 states. The Company serves larger markets including New York, Los Angeles, Chicago, Atlanta and the San Francisco Bay Area, medium-sized markets such as Salt Lake City and Nashville, and clusters of smaller markets in Orange County, California and central Pennsylvania. The Company anticipates developing additional new markets throughout a majority of the nation's top 30 markets which, together with its existing markets, are expected to have a total of approximately 27 million addressable business lines by the end of 2000. The Company plans to launch service in Dallas, Denver and Miami in the fourth quarter of 1998 and in San Diego, Washington, D.C. and Seattle in the first half of 1999. The Company is also developing a national network strategy to enable it to offer its customers complete, end-to-end voice and data communications services over NEXTLINK-owned facilities.

The table below provides selected key financial and operating data (dollars are in thousands):

	As of and For the Three Months Ended September 30, 1998	1997
Financial data:		
Gross property and equipment	$ 511,204	$ 214,320
EBITDA (1)	$ (36,576)	$ (19,844)
Operating data (2):		
Route miles (3)	2,150	1,757
Fiber miles (4)	158,987	124,399
On-net buildings connected (5)	736	479
Off-net buildings connected (6)	9,688	1,404
Switches installed	18	13
Access lines in service (7)	134,107	30,944
Employees	2,065	1,027

(1) EBITDA represents net loss before interest expense, interest income, depreciation, amortization and deferred compensation expense. EBITDA is commonly used to analyze companies on the basis of operating performance, leverage and liquidity. While EBITDA should not be construed as a substitute for operating income or a better measure of liquidity than cash flow from operating activities, which are determined in accordance with generally accepted accounting principles, it is included herein to provide additional information with respect to the ability of the Company to meet future debt service, capital expenditure and working capital requirements.

(2) The operating data includes 100% of the statistics of the Las Vegas network, which the Company manages and in which the Company has a 40% membership interest.

(3) Route miles refers to the number of miles of the telecommunications path in which the Company-owned or leased fiber optic cables are installed.

(4) Fiber miles refers to the number of route miles installed along a telecommunications path, multiplied by the Company's estimate of the number of fibers along that path.

(5) Represents buildings physically connected to the Company's networks, excluding those connected by unbundled incumbent local exchange carrier (ILEC) facilities.

(6) Represents buildings connected to the Company's networks through leased or unbundled ILEC facilities.

(7) Represents the number of access lines in service, including those lines that are provided through resale of Centrex services, for which the Company is billing services. The Company serviced 3,312 resold access lines as of September 30, 1998. The Company defines an access line as a telephone connection between a customer purchasing local telephone services and NEXTLINK. This connection does not include the concept of access line equivalents (ALEs), and is a one-for-one relationship with no multipliers used for trunk ratios, except for those trunks over which primary rate interface (PRI) service is provided, which are counted as 23 access lines.

The Company builds its networks to encompass the significant business concentrations in each area it serves, focusing on direct connections to end-user locations and ILEC central offices. The Company employs a uniform technology platform for each of its local exchange networks that is based on the Nortel DMS 500 digital local and long distance combination switching platform and associated distribution technology. As of September 30, 1998, the Company had 16 operational Nortel DMS 500 switches, including one switch in its NEXTLAB facility, and currently plans to install three additional switches by the end of 1998. NEXTLAB is a fully functional model of one of the Company's networks, which serves as a testing facility for switch software and the Company's products and services and will serve as the Company's network operations control center.

The development of the Company's businesses and the construction, acquisition and expansion of its networks require significant expenditures, substantial portions of which are incurred before the realization of revenues. These expenditures, together with the associated early operating expenses, result in negative cash flow until an adequate customer base is established. However, as the customer base grows, the Company expects that incremental revenues can be generated with decreasing incremental operating expenses, which may provide positive contributions to cash flow. The Company has made the strategic decision to build high capacity networks with broad market coverage, which initially increases its level of capital expenditures and operating losses. The Company believes that over the long term this will enhance the Company's financial performance by increasing the traffic flow over the Company's networks. The Company has recently entered into leased dark fiber and fiber capacity arrangements which allow the Company, by installing one or more switches and related electronics, to enter a market prior to completing construction of its own fiber optic network.

RESULTS OF OPERATIONS

Revenue increased 182% to $37.8 million during the third quarter of 1998, from $13.4 million in the same period in 1997. Year to date revenue of $96.4 million represented a 175% increase from the $35.1 million reported for the comparable period in 1997. The increase was driven by 290% growth in revenues from bundled local and long distance services and dedicated services, as well as by the acquisitions of Start Technologies Corporation (Start) and Chadwick Telecommunications Corporation (Chadwick) in the fourth quarter of 1997. Revenues reported in the third quarter of 1998 included $31.5 million derived from local and long distance, competitive access, dedicated line services and shared tenant services and $6.3 million derived from enhanced communications services, primarily interactive voice response (IVR) services. The Company's IVR revenue comprised 16% and 28% of the Company's total revenues during the third quarter of 1998 and 1997, respectively.

The Company increased the number of customer access lines added during the quarter from 30,053 in the second quarter of 1998 to 31,220 during the third quarter of 1998. As of September 30,1998, the Company had 134,107 access lines in service, compared to 50,131 as of December 31, 1997 and 30,944 as of September 30, 1997. Revenues from the provision of such services are expected to continue to increase as a component of total revenues over future periods. Access lines in service includes those lines which are provided through resale of Centrex services, the number of which is decreasing over time as the Company converts those customers to its own network.

Operating expenses consist of costs directly related to providing facilities-based network and enhanced communications services and also include salaries and benefits and related costs of operations and engineering personnel. Operating expenses increased 136% in the third quarter of 1998 to $32.8 million, an increase of $18.9 million over the third quarter of 1997. For the nine months ended September 30, 1998, operating expenses rose $49.6 million, or 138%, over the same period in 1997. These increases were attributed to increased network costs related to provisioning higher volumes of local, long distance and enhanced communications services, an increase in employees and an increase in other related costs primarily to expand the Company's switched local and long distance service businesses in its existing and planned markets. To a lesser extent, the acquisitions of Start and Chadwick in the fourth quarter of 1997 also contributed to the increase in operating costs over those in the third quarter of 1997.

Selling, general and administrative (SG&A) expenses include salaries and related personnel costs, facilities expenses, sales and marketing, information systems costs, consulting and legal fees and equity in loss of affiliates. SG&A expenses increased 115% and 126% in the three and nine-month periods ended September 30, 1998 as compared to the corresponding periods in 1997. The increases were due to the Company's increase in employees, as well as other costs associated with the expansion of the Company's switched local and long distance service businesses in its existing and planned markets.

Deferred compensation expense was recorded in connection with the Company's Equity Option Plan until April 1997, and in connection with the Company's Stock Option Plan, which replaced the Equity Option Plan, subsequent to April 1997. The stock options granted under the Equity Option Plan were considered compensatory and were accounted for on a basis similar to that for stock appreciation rights. All options outstanding under the Equity Option Plan were regranted under the new Stock Option Plan with terms and conditions substantially the same as under the Equity Option Plan. As such, the Company continues to record deferred compensation expense for those compensatory stock options issued, as well as for compensatory stock options issued subsequent to the Plan conversion date. Compensation expense is recognized over the vesting periods based on the excess of the fair value of the stock options at the date of grant over the exercise price.

Depreciation expense increased primarily due to placement in service of additional telecommunications network assets, including switches, fiber optic cable, network electronics and related equipment. Amortization of intangible assets increased primarily as a result of the Start and Chadwick acquisitions in the fourth quarter of 1997.

Interest expense increased 248% in the third quarter of 1998 over the comparable period in the prior year due to an increase in the Company's average outstanding indebtedness over the respective periods. Interest expense will increase in future periods in conjunction with the sale of $500.0 million in aggregate principal amount of 10¾% Senior Notes on November 12, 1998. See "—Liquidity and Capital Resources." Pursuant to Statement of Financial Accounting Standards No. 34, the Company capitalizes a portion of its interest costs as part of the construction cost of its communications networks. Capitalized interest during the first nine months of 1998 totaled $3.0 million. Interest income results from investment of excess cash as well as certain securities that have been pledged as collateral for interest payments on the 12½% Senior Notes. The increase in interest income for the three and nine-month periods in 1998 over the same periods in 1997 corresponded to the increase in the Company's average outstanding cash balances.

LIQUIDITY AND CAPITAL RESOURCES

The competitive local telecommunications service business is a capital-intensive business. The Company's existing operations have required and will continue to require substantial capital investment for the acquisition and installation of fiber, electronics and related equipment in order to provide switched services in the Company's networks and the funding of operating losses during the start-up phase of each market. In addition, the Company's strategic plan calls for expansion into additional market areas. Such expansion will require significant additional capital for: potential acquisitions of businesses or assets; design, development and construction of new networks; and the funding of operating losses during the start-up phase of each market. During the first nine months of 1998, the

Company used $104.8 million in cash for operating activities, compared to $59.2 million for the same period in the prior year. The increase was primarily due to a substantial increase in the Company's activities associated with the continued development and expansion of switched local and long distance service operations. During the first nine months of 1998, the Company invested an additional $301.1 million in property and equipment and acquisitions of telecommunications assets. During the same period in 1997, the Company invested $130.7 million in property and equipment, acquisitions of telecommunications assets and businesses and equity investments in telecommunications businesses.

In July 1998, the Company announced the formation of INTERNEXT L.L.C., which is beneficially owned 50% each by the Company and Eagle River Investments, L.L.C (Eagle River). INTERNEXT entered into an agreement with Level 3 Communications LLC (Level 3). Level 3 is constructing a national fiber optic network that is expected to cover more than 16,000 route miles with six or more conduits and connect 50 cities in the United States and Canada. Pursuant to this agreement, INTERNEXT will receive an exclusive interest in 24 fibers in a shared, filled conduit, one entire empty conduit and the right to 25% of the fibers pulled through the sixth and any additional conduits in the network. INTERNEXT will pay $700.0 million in exchange for these rights, the majority of which will be payable as segments of the network are completed and accepted by INTERNEXT, which is expected to occur substantially during 2000 and 2001. The Company has guaranteed 50% of the financial obligations of INTERNEXT under this agreement and, together with Eagle River, has also guaranteed the performance of certain other obligations of INTERNEXT thereunder. The Company anticipates that Nextel Communications, Inc. (Nextel) will acquire a one-third ownership interest in INTERNEXT, which would reduce the Company's beneficial ownership interest in and obligations with respect to INTERNEXT to one-third. The Company is in the process of defining its plans for implementation of a national network strategy, which will require additional capital expenditures.

In February 1998, the Company signed a definitive agreement with Metromedia Fiber Network for exclusive rights to multiple fibers and innerducts for 20 years, with two 10-year renewals. The route covered by the agreement extends from Manhattan to White Plains (NY), to Stamford (CT), to Newark (NJ) and south from Manhattan through Philadelphia, Wilmington (DE), Baltimore, and to Washington (DC). The route will offer frequent splice points within metropolitan areas and on routes between metropolitan areas, as well as provide access to ILEC central and tandem switching offices. The Company paid $92.0 million in cash for this transaction, $80.3 million of which was placed into escrow, to be released as segments of the route are constructed and delivered to the Company.

In January 1998, the Company and Nextel formed NEXTBAND, a joint venture that is owned 50% each by the Company and Nextel. NEXTBAND was the successful bidder in 42 markets in the FCC's local multipoint distribution service (LMDS) auctions. The Company's pro rata share of NEXTBAND's total bid in the LMDS auctions was $67.4 million, which was paid in full in June 1998. The Company is in process of defining its operational and financial plans for implementation of an LMDS strategy, which will likely involve additional capital expenditures.

On March 3, 1998, the Company completed the sale of $335.0 million in aggregate principal amount of 9% Senior Notes due March 15, 2008. Proceeds from the sale net of discounts, underwriting commissions, advisory fees and expenses totaled approximately $326.5 million. Interest payments on the 9% Senior Notes are due semi-annually, beginning September 1998.

On March 31, 1998, the Company completed the sale of 4,000,000 shares of 6½% cumulative convertible preferred stock (6½% Preferred Stock) with a liquidation preference of $50 per share. The sale generated gross proceeds to the Company of $200.0 million, and proceeds net of underwriting discounts, advisory fees and expenses of $193.8 million. Each share of 6½% Preferred Stock is convertible, at the option of the holder, into 1.145 shares of the Company's Class A common stock (subject to adjustments in certain circumstances). Dividends on the 6½% Preferred Stock accrue from March 31, 1998 and are payable quarterly in cash, beginning on June 30, 1998.

On April 1, 1998, the Company completed the sale of 9.45% Senior Discount Notes (9.45% Notes), due April 15, 2008. The 9.45% Notes were issued at a discount from their principal amount to generate aggregate gross proceeds to the Company of approximately $400.0 million. Proceeds net of underwriting commissions, advisory fees and expenses totaled $390.9 million. The 9.45% Notes accrete at a rate of 9.45% compounded semi-annually, to an aggregate principal amount of approximately $637.0 million by April 15, 2003. No cash interest will accrue on the Notes until April 15, 2003. Interest will become payable in cash semi-annually beginning on October 15, 2003.

On November 12, 1998, the Company completed the sale of $500.0 million in aggregate principal amount of 10¾% Senior Notes due November 15, 2008. Proceeds from the sale net of underwriting commissions, advisory fees and expenses totaled approximately $488.5 million. Interest payments on the notes are due semi-annually, beginning May 1999. Pursuant to a covenant in the indenture under which the 10¾% Senior Notes were issued, the Company has agreed to use the net proceeds from the sale for expenditures relating to the construction, improvement and acquisition of new and existing networks and services and direct or indirect investments in certain joint ventures (including NEXTBAND and INTERNEXT) to fund similar expenditures.

The Company will use the net proceeds from the sale of the 9% Senior Notes, the 6½% Preferred Stock, the 9.45% Notes, the 10¾% Senior Notes (subject to the limitations described above) and existing unrestricted cash balances for expenditures relating to the development, construction, acquisition and operation of telecommunications networks and service providers and the offering of telecommunications services in those areas where the Company currently operates or intends to operate. Expenditures for the construction and operation of networks include (i) the purchase and installation of switches and related electronics in existing networks and in networks to be constructed or acquired in new or adjacent markets, (ii) the purchase and installation of fiber optic cable and electronics to expand existing networks and develop new networks, including the connection of new buildings, (iii) the development of its comprehensive information technology platform, (iv) the acquisition of LMDS spectrum purchased in the FCC's auction and the construction and deployment of associated facilities and (v) the funding of operating losses and working capital. The Company may also acquire or invest in businesses that consist of existing networks or companies engaged in businesses similar to those engaged in by the Company and its subsidiaries or other complementary businesses.

As of September 30, 1998, the Company had unrestricted cash and investments of $1,176.8 million and $1,665.3 million on a pro forma basis after giving effect to the sale of the 10¾% Senior Notes. The Company's current plan contemplates an aggressive expansion into a number of new markets throughout the United States. The Company may pursue various alternatives for achieving its growth strategy, including: additional network construction; additional leases of network capacity from third party providers; acquisitions of existing networks; and spectrum that was purchased during the LMDS auction and associated facilities construction and deployment. The Company also anticipates that a substantial amount of additional capital expenditures will be made in 1999 and beyond. The funding of these capital expenditures is expected to be provided by existing cash balances, future vendor and/or credit facilities, future public or private sales of debt securities, future sales of public or private capital stock and joint ventures. There can be no assurance, however, that the Company will be successful in raising sufficient additional capital on terms that it will consider acceptable or that the Company's operations will produce positive consolidated cash flow in sufficient amounts to meet its interest and dividend obligations on its outstanding securities. Failure to raise and generate sufficient funds may require the Company to delay or abandon some of its planned future expansion or expenditures, which could have a material adverse effect on the Company's growth and its ability to compete in the telecommunications services industry.

In addition, the Company's operating flexibility with respect to certain business matters is, and will continue to be, limited by covenants associated with the 12½% Senior Notes, the 9 5/8% Senior Notes, the 9% Senior Notes, the 9.45% Notes and the 10¾% Senior Notes (collectively referred to as the Notes). Among other things, these covenants limit the ability of the Company and its subsidiaries to incur additional indebtedness, create liens upon assets, apply the proceeds from the disposal of assets, make dividend payments and other distributions on capital stock and redeem capital stock. In addition, the terms of the 14% Senior Exchangeable Redeemable Preferred Shares (14% Preferred Shares) contain certain covenants that may limit the Company's operating flexibility with respect to the incurrence of indebtedness and issuance of additional preferred shares. There can be no assurance that such covenants will not adversely affect the Company's ability to finance its future operations or capital needs or to engage in other business activities that may be in the interest of the Company. The Company was in compliance with all covenants associated with the Notes and the 14% Preferred Shares as of September 30, 1998.

IMPACT OF YEAR 2000

Certain of the Company's older computer systems and applications were written to define a given year with abbreviated dates using the last two digits in a year rather than the entire four digits. As a result, when computer systems attempt to process dates both before and after January 1, 2000, two digit year fields may create processing ambiguities that can cause errors and system failures. For example, systems and applications may have time-sensitive software that recognize an abbreviated year "00" as the year 1900 rather than the year 2000. These errors or failures may have limited effects, or the effects may be widespread, depending on the computer chip, system, or software, and its location and function.

State of Readiness

The Company is currently assessing the impact of the Year 2000, and a formal Year 2000 plan (the "Plan") in expected to be completed and adopted by the Company by year-end 1998. The purpose of the Plan will be to develop and perform reasonable steps intended to prevent the Company's critical operational functions from being impaired due to the Year 2000 problem. The first phase of the Company's Year 2000 assessment, to be completed by December 1998, includes: 1) taking an inventory of Company-wide systems and equipment to determine the extent of testing required for Year 2000 compliance (generally defined as the ability of information systems to accurately process data from, into and between the twentieth and twenty-first centuries, including leap year calculations), 2) developing a strategy to manage vendors' and other outside entities' progress toward Year 2000 compliance, 3) designing a Company-wide Year 2000 communications plan, and 4) creating a risk assessment and impact analysis from which the Plan can be developed. The Company has engaged outside consultants to aid in formulating and implementing the Plan.

The Company's assessments to date have indicated that its major operational support systems, including its billing, order management, network management, and financial systems are Year 2000 compliant. In addition, the Company has received positive confirmation from its vendor that the Company's Nortel DMS 500 switches are also Year 2000 compliant.

As part of the Plan and ongoing Year 2000 assessment, the Company will continue its testing of existing telecommunications equipment and back office systems to assess the effects of the Year 2000 problem on those areas that would result in significant impairment to the Company's critical operations. Through its NEXTLAB facility, which operates separate and apart from the Company's operational switches, the Company has the means to test switch configurations without impacting its networks or customers, and the Company is using NEXTLAB to independently verify Year 2000 compliance of its network systems and equipment.

The Plan will also address the potential adverse effects to the Company in the event that the computer, telecommunications, and other systems of outside entities' (including vendors, customers, and local and interexchange carriers and Internet service providers with which the Company interchanges traffic) are not Year 2000 compatible. The Company does not have control of these outside entities or their systems. However, the Company's Plan will include ongoing identification of and contact with such outside entities whose systems may have a substantial effect on the Company's ability to continue to conduct the critical aspects of its operations without disruption from Year 2000 problems. In the event such outside systems are identified, the Company will work with the outside entities in a reasonable attempt to inventory, assess, analyze, test, and develop contingency plans for the Company's connections to these outside entities and their systems and to determine the extent to which they are, or can be made to be, Year 2000 compliant.

Costs to Address Year 2000 Issues

The Company has not incurred material historical costs for Year 2000 awareness, inventory, assessment, analysis, conversion, testing, or contingency planning. Further, the Company anticipates that its future costs for these purposes will not be material.

Year 2000 costs are difficult to estimate accurately because of unanticipated vendor delays, technical difficulties, the impact of tests of outside entities' systems, and similar events. Although management believes that its estimates are reasonable, there can be no assurance that the actual costs of implementing the Plan will not differ materially from the estimated costs or that the Company will not be materially adversely affected by Year 2000 issues. Furthermore, the estimated costs of implementing the Plan do not consider the costs, if any, that might be incurred as a result of Year 2000-related failures that occur despite the Company's implementation of the Plan.

Year 2000 Risk Factors

Between now and the year 2000 there will be increased competition for people with the technical and managerial skills necessary to deal with the Year 2000 problem. The Company believes it employs an adequate number personnel skilled in dealing with the Year 2000 problem and has retained outside consultants who bring additional skilled people to deal with the Year 2000 problem as it affects the Company. Nevertheless, the Company could face shortages of skilled personnel or other resources, such as Year 2000 compliant computer chips. These shortages might delay or otherwise impair the Company's ability to assure that its critical systems are Year 2000 compliant. Outside entities could face similar problems that could materially affect the Company. The Company believes that the possible impact of the shortage of skilled people and resources is not, and will not be, unique to the Company.

The Company believes that its critical systems will be Year 2000 compliant before January 1, 2000. However, there is no assurance that the Plan will succeed in accomplishing its purposes and unforeseen circumstances may arise during implementation of the Plan that would materially and adversely affect the Company.

The Company is taking reasonable steps to identify, assess, and, where appropriate, replace devices that contain embedded chips. Despite these reasonable efforts, the Company may not be able to find and remediate all embedded chips in all of the Company's systems. Further, outside entities on which the Company depends also may not be able to find and remediate all embedded chips in their systems. Some chips that are not Year 2000 compliant may create system disruptions or failures, which may, in turn, cause disruptions or failures in other systems. These cascading problems could impair the Company's ability to serve its customers and otherwise fulfill contractual and legal obligations. The Company believes that the possible adverse impact of the embedded chip problem is not, and will not be, unique to the Company.

The Company cannot ensure that suppliers upon which it depends for essential supplies and services will convert and test their critical systems and processes in a timely manner. Failure or delay by all or some of these entities, including federal, state, or local governments, to make their systems and processes Year 2000 compliant could create substantial disruptions having a material adverse effect on the Company's operations.

In a recent Securities and Exchange Commission release regarding Year 2000 disclosure, the Securities and Exchange Commission stated that public companies must disclose the most reasonably likely worst case Year 2000 scenario. Although it is not possible to assess the likelihood of any of the following events, each must be included in a consideration of worst case scenarios: widespread failure of electrical, gas, and similar supplies serving the Company; widespread disruption of the services provided by common communications carriers; similar disruption to the means and modes of transportation for the Company and its employees, contractors, suppliers, and customers; significant disruption to the Company's ability to gain access to, and remain working in, office buildings and other facilities; the failure of substantial numbers of the Company's critical computer hardware and software systems, including both internal business systems and systems controlling operational facilities such as electrical generation, transmission, and distribution systems; and the failure of outside entities' systems, including systems related to banking and finance. Among other things, the Company could face substantial claims by customers or loss of revenue due to service interruptions, inability to fulfill contractual obligations or to bill customers accurately and on a timely basis, and increased expenses associated with litigation, stabilization of operations following critical system failures, and the execution of contingency plans. The Company could also experience an inability by customers and others to pay, on a timely basis or at all, obligations owed to the Company. Under these circumstances, the adverse effects on the Company would be material, although not quantifiable at this time. Further, the cumulative effect of these failures could have a substantial adverse effect on the economy, domestically and internationally. The adverse effect on the Company from a domestic or global recession or depression also could be material, although not quantifiable at this time.

The Company will continue to monitor business conditions to assess and quantify material adverse effects, if any, that may result from the Year 2000 problem.

Contingency Plans

As part of the Plan, the Company is developing contingency plans that deal with two aspects of the Year 2000 problem: 1) that the Company, despite its good faith and reasonable efforts, may not have satisfactorily addressed the Year 2000 problem with respect to its critical internal systems and 2) that outside entities' systems may not be Year 2000 ready. The Company's contingency plans will be designed to minimize the disruptions or other adverse effects resulting from Year 2000 incompatibilities with respect to critical functions or systems.

The Company's contingency plans will contemplate an assessment of all its critical internal information technology systems and its internal operational systems that use computer-based controls. In addition, the Company will assess any critical disruptions due to Year 2000-related failures that are external to the Company. These processes will begin January 1, 2000, and will continue as long as circumstances require.

The Company's contingency plans will include the creation of teams that will be prepared to respond immediately and as necessary to critical Year 2000 problems as soon as they become known. The composition of teams that are assigned to deal with such problems will vary according to the nature, significance, and location of the problem.

INFORMATION REGARDING FORWARD LOOKING STATEMENTS

The statements contained in this report and in associated prior filings by the Company with the Securities and Exchange Commission which are not historical facts are "forward-looking statements" (as such term is defined in the Private Securities Litigation Reform Act of 1995), which can be identified by the use of forward-looking terminology such as "believes", "expects", "may", "will", "should", or "anticipates" or the negative thereof or other variations thereon or comparable terminology, or by discussions of strategy that involve risks and uncertainties. Such forward-looking statements include, but are not limited to: the Company's plans to build, acquire or develop networks and offer services in new areas, expand its current networks and explore the acquisition or licensing of additional enhanced communications services and other telecommunications service providers (and the effects of such efforts); the Company's development of a national strategy for end-to-end communications services; the Company's presence in the marketplace and its ability to provide a single source solution for the telecommunications needs of its customers; the Company's anticipated development of and entry into new markets and market expansion (and timing thereof); its expected number of addressable business lines in markets where the Company operates and by the end of 2000; its plans to launch service in various cities; its plans to install additional switches by the end of 1998; its expectation regarding incremental revenues, incremental operating expenses and contributions to cash flow; the Company's belief regarding its financial performance and traffic flow over its networks; its expectations regarding revenue from access lines as a percentage of total revenues; increases in interest expense in future periods; its requirements for capital investment; its use of proceeds from various financings; its anticipated capital expenditures; its intentions regarding LMDS technology; matters related to the national network being constructed by Level 3, including network specifications, INTERNEXT's interest therein, the delivery of segments thereunder, and the cost thereof and the timing of payments for the network; the participation by other entities (including Nextel) in certain joint ventures and financial matters related thereto; and other statements contained herein regarding matters that are not historical facts. Management wishes to caution the reader that these forward-looking statements are only predictions. These statements are based on a number of assumptions that ultimately could prove inaccurate and, therefore, no assurance can be given that the future results will be achieved. Actual events or results may differ materially as a result of a number of factors, including those identified in the Company's annual report on Form 10-KSB (File No. 333-04603). Factors that could affect performance include: the level of the Company's future negative cash flows and operating losses incurred by the Company until it establishes an adequate revenue base and generates substantial revenues from the provision of switched local and long distance services; successfully generating or raising on terms that the Company will consider acceptable sufficient capital to accommodate planned future expansion and expenditures; continued attraction and retention of qualified managerial, professional and technical personnel; timely installation of the required switches, fiber optic cable and associated electronics necessary to provide switched local service in a manner that will permit the resolution of technical problems; successfully negotiating new and, to the extent necessary, renegotiating existing interconnection agreements; successfully developing effective systems relating to ordering, provisioning and billing for telecommunications services; successfully offering, marketing and selling switched local services and other enhanced products and services in all of the Company's networks as quickly as practicable; sufficient access to the ILEC's networks and adequate cooperation therefrom to connect new customers to the Company's network on a timely basis; identifying, financing and completing suitable acquisitions; maintaining existing, and obtaining and maintaining new, franchises, permits and rights-of-way and any required governmental authorizations, franchises and permits on a timely basis; competition from incumbent providers and new entrants; the nature of regulatory, legislative and judicial developments; rapid and significant changes in technology; and risks related to the Company's national network and LMDS strategies. These are representative of factors that could affect the outcome of the forward-looking statements. In addition, such statements could be affected by general industry and market conditions and economic conditions including interest rate fluctuations.

NEW ACCOUNTING STANDARD

In April 1998, the AICPA released Statement of Position 98-5, "Reporting on the Costs of Start-Up Activities" (SOP 98-5). The new standard requires that all entities expense costs of start-up activities as those costs are incurred. SOP 98-5 defines "start-up costs" as those costs directly related to pre-operating, pre-opening, and organization activities. This standard must be adopted in fiscal years beginning after December 15, 1998. The adoption of SOP 98-5 will not have a material impact the Company's financial position.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company is not currently a party to any legal proceedings, other than regulatory and other proceedings that are in the normal course of its business.

Item 2. Changes in Securities and Use of Proceeds

The Company filed a registration statement on Form S-1 (File No. 333-32001) which became effective on September 26, 1997, whereby 15,200,000 shares of Class A common stock, $.02 par value per share, were sold in an initial public offering (IPO) at a price of $17 per share. Of the 15,200,000 shares of Class A common stock sold, 12,000,000 were sold by the Company and 3,200,000 were sold by a selling shareholder. The Company did not receive any of the proceeds from the sale of shares by the selling shareholder. In addition, the underwriters of the IPO, led by Salomon Brothers Inc, exercised an option to purchase 2,280,000 additional shares of Class A common stock at the same price per share. Net proceeds to the Company from the initial public offering totaled approximately $226.8 million, after deducting underwriting discounts, advisory fees and expenses aggregating approximately $16.0 million. The Company intends to use substantially all of the net proceeds from the initial public offering for expenditures relating to the expansion of existing networks and services, the development and acquisition of new networks and services and the funding of operating losses and working capital. None of the proceeds from this offering had been used as of September 30, 1998.

The Company filed a registration statement on Form S-1 (File No. 333-32003) which became effective on September 26, 1997, whereby the Company sold $400.0 million aggregate principal amount of 9 5/8% Senior Notes. The offering was led by Salomon Brothers Inc. Net proceeds from the sale of the 9 5/8% Senior Notes totaled approximately $388.5 million, after deducting issuance costs aggregating approximately $11.5 million, relating to underwriting discounts, advisory fees and expenses. The use of proceeds from the debt offering is expected to be substantially the same as the Company's initial public offering. Approximately $349.8 million of the proceeds from this offering had been used as of September 30, 1998, $209.1 million of which was used for the purchase of property and equipment, $20.5 million for the network lease agreement entered into in February 1998, and the remainder was used to fund the Company's operations and working capital requirements.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

3.1 Certificate of Incorporation of NEXTLINK Communications, Inc. (1)

3.2 By-laws of NEXTLINK Communications, Inc. (1)

PART II. OTHER INFORMATION

3.3	Articles of Incorporation of NEXTLINK Capital, Inc. (2)
3.4	By-laws of NEXTLINK Capital, Inc. (2)
4.1	Form of Exchange Note Indenture, by and among NEXTLINK Communications, Inc. and United States Trust Company of New York, as Trustee, relating to the Exchange Notes, including form of Exchange Notes. (3)
4.2	Certificate of Designations of the Powers, Preferences and Relative, Participating, Optional and Other Special Rights of 14% Senior Exchangeable Redeemable Preferred Shares and Qualifications, Limitations and Restrictions Thereof. (1)
4.3	Form of stock certificate of 14% Senior Exchangeable Redeemable Preferred Shares. (3)
4.4	Indenture, dated as of April 25, 1996, by and among NEXTLINK Communications, Inc., NEXTLINK Capital, Inc. and United States Trust Company of New York, as Trustee, relating to 12½% Senior Notes due April 15, 2006, including form of global note. (2)
4.5	First Supplemental Indenture, dated as of January 31, 1997, by and among NEXTLINK Communications, Inc., NEXTLINK Communications, L.L.C., NEXTLINK Capital and United States Trust Company of New York, as Trustee. (3)
4.6	Form of Indenture between United States Trust Company, as Trustee and NEXTLINK Communications, Inc., relating to the 9 5/8% Senior Notes due 2007. (4)
4.7	Indenture, dated March 3, 1998, between United States Trust Company, as Trustee and NEXTLINK Communications, Inc., relating to the 9% Senior Notes due 2008. (5)
4.8	Certificate of Designations of the Powers, Preferences and Relative, Participating, Optional and Other Special Rights of 6½% Cumulative Convertible Preferred Stock and Qualifications, Limitations and Restrictions Thereof. (1)
4.9	Indenture, dated April 1, 1998, between United States Trust Company, as Trustee and NEXTLINK Communications, Inc. relating to the 9.45% Senior Discount Notes due 2008. (6)
4.10	Second Supplemental Indenture, dated June 3, 1998, amending Indenture dated April 25, 1996, by and among NEXTLINK Communications, Inc., NEXTLINK Capital, Inc. and United States Trust Company of New York, as Trustee. (1)
4.11	First Supplemental Indenture, dated June 3, 1998, amending Indenture dated September 25, 1997, by and between NEXTLINK Communications, Inc. and United States Trust Company of New York, as Trustee. (1)
4.12	First Supplemental Indenture, dated June 3, 1998, amending Indenture dated March 3, 1998, by and between NEXTLINK Communications, Inc. and United States Trust Company of New York, as Trustee. (1)

PART II. OTHER INFORMATION

4.13	Cost Sharing and IRU Agreement dated July 18,1998, between Level 3 Communications, LLC and INTERNEXT LLC. (7)
10.1	Stock Option Plan of NEXTLINK Communications, Inc., as amended. (1)
10.2	Employee Stock Purchase Plan of NEXTLINK Communications, Inc. (1)
10.3	Registration Rights Agreement dated as of January 15, 1997, between the predecessor of NEXTLINK Communications, Inc. and the signatories listed therein. (3)
10.4	Preferred Exchange and Registration Rights Agreement, dated as of January 31, 1997, by and among the predecessor of NEXTLINK Communications, Inc. and the Initial Purchasers. (3)
10.5	Fiber Lease and Innerduct Use Agreement, dated as of February 23, 1998, by and between NEXTLINK Communications, Inc. and Metromedia Fiber Network, Inc. (5)
10.6	Amendment No. 1 to Fiber Lease and Innerduct Use Agreement, dated as of March 4, 1998, by and between NEXTLINK Communications, Inc. and Metromedia Fiber Network, Inc. (5)
10.7	Guaranty Agreement, dated July 18, 1998, between NEXTLINK Communications, Inc. and Level 3 Communications, LLC.
10.8	Cost Sharing and IRU Agreement, dated July 18, 1998, between Level 3 Communications, LLC and INTERNEXT LLC. (7)
27	Financial Data Schedule

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(1) Incorporated herein by reference to the exhibit filed with the Registration Statement on Form S-4 of NEXTLINK Communications, Inc. and NEXTLINK Capital, Inc. (Commission File No. 333-53975).

(2) Incorporated herein by reference to the exhibit filed with the Registration Statement on Form S-4 of NEXTLINK Communications, L.L.C. (the predecessor of NEXTLINK Communications, Inc.) and NEXTLINK Capital, Inc. (Commission File No. 333-4603).

(3) Incorporated herein by reference to the exhibit filed with the Annual Report on Form 10-KSB for the year ended December 31, 1996 of NEXTLINK Communications, Inc. and NEXTLINK Capital, Inc. (Commission File Nos. 333-04603 and 333-04603-01).

(4) Incorporated herein by reference to the exhibit filed with the Registration Statement on Form S-1 of NEXTLINK Communications, Inc. (Commission File No. 333-32003).

(5) Incorporated herein by reference to the exhibit filed with the Annual Report on Form 10-KSB for the year ended December 31, 1997 of NEXTLINK Communications, Inc. and NEXTLINK Capital, Inc. (Commission File Nos. 333-04603 and 333-04603-01).

(6) Incorporated herein by reference to the exhibit filed with the quarterly report on Form 10-Q for the quarterly period ended March 31, 1998 of NEXTLINK Communications, Inc. and NEXTLINK Capital, Inc. (Commission File No. 000-22939).

(7) Portions of this exhibit were omitted and filed separately with the Secretary of the Commission pursuant to NEXTLINK Communications, Inc.'s Application Requesting Confidential Treatment under Rule 24(b)-2 of the Securities Exchange Act of 1934.

PART II. OTHER INFORMATION

(b) Reports on Form 8-K

Current report on Form 8-K, filed July 20, 1998, regarding the announcement by James Voelker of his resignation as President and a director of the Company and the appointment of George Tronsrue as President of the Company.

Current report on Form 8-K, filed July 22, 1998, regarding INTERNEXT L.L.C., of which each of the Company and Eagle River Investments L.L.C. beneficially owns a one-half interest, entering into a Cost Sharing and IRU Agreement with Level 3 Communications, LLC.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrants have duly caused this report to be signed on their behalf by the undersigned thereunto duly authorized.

NEXTLINK Communications, Inc.

Date: November 16, 1998

By: /s/ Kathleen H. Iskra
Kathleen H. Iskra
Vice President, Chief Financial Officer and Treasurer
(Principal financial and accounting officer)

NEXTLINK Capital, Inc.

Date: November 16, 1998

By: /s/ Kathleen H. Iskra
Kathleen H. Iskra
Vice President, Chief Financial Officer and Treasurer
(Principal financial and accounting officer)

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-KSB

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 1997
Commission File Nos. 333-04603 and 333-04603-01

NEXTLINK COMMUNICATIONS, INC.

A Washington Corporation I.R.S. Employer No. 91-1738221

NEXTLINK CAPITAL, INC.

A Washington Corporation I.R.S. Employer No. 91-1716062

155 108th Avenue, N.E., 8th Floor, Bellevue, Washington 98004
Telephone Number (425) 519-8900

Securities registered pursuant to Section 12(b) of the Act:
NONE

Securities registered pursuant to Section 12(g) of the Act:
Class A Common Stock, Par Value $0.0227

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Registration S-B is not contained herein, and will not be contained, to the best of Registrants' knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-KSB or any amendment to this Form 10-KSB. ☐

The Issuers' revenues for its most recent fiscal year were $57,579,000.

The aggregate market value of the Class A and Class B Common Stock held by non-affiliates of the Issuers, based upon the closing sale price of the Common Stock on March 6, 1998 as reported on the NASDAQ National Market System, was approximately $706,098,643. Shares of Class A and Class B Common Stock held by each executive officer and director and by each person who owns 5% or more of the outstanding Class A and Class B Common Stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of March 6, 1998, the number of outstanding shares of NEXTLINK Communications, Inc.'s Class A Common Stock was 19,249,940 and Class B Common Stock was 34,247,644. NEXTLINK Capital, Inc. had outstanding 1,000 shares of Common Stock, par value $0.01 per share.

NEXTLINK Capital, Inc. ("NEXTLINK Capital" and together with the Company, the "Issuers") meets the conditions set forth in General Instruction G(1)(a) and (b) of Form 10-KSB and is therefore filing this form with the reduced disclosure format.

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NEXTLINK Communications, Inc.
NEXTLINK Capital, Inc.

PART I

Item 1. *Description of Business*

Capitalized terms used herein which are not otherwise defined have the respective meanings ascribed to them in the Glossary, beginning on page 19.

Overview

NEXTLINK Communications, Inc. ("NEXTLINK" or the "Company") was founded in 1994 by Craig O. McCaw, its largest and controlling shareholder, to provide local facilities-based telecommunications services to its targeted customer base of small and medium-sized businesses. In July 1996, NEXTLINK became one of the first competitive local exchange carriers ("CLECs") in the United States to provide facilities-based switched local services under the Telecommunications Act of 1996 (the "Telecom Act"), which opened the entire local exchange market to competition. In each of the markets it serves, NEXTLINK seeks to become a principal competitor to the incumbent local exchange carrier ("ILEC") for its targeted customers by providing an integrated package of high quality local, long distance and enhanced telecommunications services at competitive prices. In October 1997, the Company completed an initial public offering of shares of its Class A Common Stock.

The market potential for competitive telecommunications services is large and growing. Industry sources estimate that in 1996 the total revenues from local and long distance telecommunications services were approximately $183 billion, of which approximately $101 billion were derived from local exchange services and approximately $82 billion from long distance services. Based upon FCC information, aggregate revenues for local and long distance services grew at a compounded annual rate of approximately 5.5% between 1991 and 1996. The Telecom Act, the FCC's issuance of rules for competition and pro-competitive policies developed by state regulatory commissions, has created opportunities for new entrants, including the Company, to capture a portion of the ILEC's dominant, and historically monopoly controlled, market share of local services. The development of switched local services competition, however, is in its early stages, and the Company believes that CLECs currently serve fewer than 5% of the total business lines in the United States.

The Company's targeted customer base within the national telecommunications market is small to medium-sized businesses, generally those businesses with fewer than 50 access lines. Based on consultants' reports, the Company estimates that as of year end 1996, there were approximately 170 million access lines nationwide, including approximately 55 million business lines.

The Company develops and operates high capacity, fiber optic networks with broad market coverage in a growing number of markets across the United States. In its switched local service markets, the Company offers its customers a bundled package of local and long distance services and also offers dedicated transmission and competitive access services to long distance carriers and end users. In addition, NEXTLINK offers several non-network-based enhanced communications services to customers nationwide, including a variety of interactive voice response ("IVR") products.

The Company currently operates 16 facilities-based networks providing switched local and long distance services in 26 markets in eight states. The Company anticipates developing additional new markets during 1998 which, together with its existing markets, are expected to have a total of approximately 15 million addressable business lines by the end of 1998. The Company's goal is to add or expand markets to increase its addressable business lines for markets in service or under development to approximately 21 million by the end of 1999.

The Company's goal of targeting 15 million addressable business lines by year end 1998 represents a 36% increase over the Company's previous objective. The Company has increased its line targets based principally on three factors: initial success in establishing networks and launching services in major metropolitan markets in Los Angeles, Chicago and Philadelphia; the Company's significant growth in the sale and installation of access lines throughout all markets; and the Company's review of several potential target markets, which underlined the significant market opportunities available to NEXTLINK in those markets.

NEXTLINK is pursuing its targeted customer base in markets of all sizes. In larger markets, the Company has operational networks in Los Angeles, Chicago and Philadelphia, and networks under development in New York City, the San Francisco Bay Area and Atlanta. The Company also has operational networks in medium-sized markets such as Las Vegas and Nashville as well as smaller markets that have been clustered in Orange County, California and central Pennsylvania. The Company will enter large markets on a stand-alone basis where it is economically attractive to do so and where competitive and other market factors warrant such entry. The Company also considers pursuing smaller markets where it can extend or cluster an existing network with relatively little incremental capital. The Company anticipates that the addressable business lines in the larger markets that it is currently operating and developing will represent the majority of the Company's addressable business lines by year end 1998 and 1999.

NEXTLINK has experienced significant growth in its customer base. NEXTLINK's customer access lines in service have increased from 8,511 access lines at December 31, 1996 to 50,131 access lines at December 31, 1997. This growth is attributable to both new network launches as well as significant increases in growth rates in those markets where the Company launched service in 1996. For markets launched in 1996, the Company has increased its access lines in service by 248%, from 8,511 to 29,591 at December 31, 1996 and 1997, respectively, representing 51% of the Company's overall increase in access lines in service over the respective periods. The Company has also improved the quarterly rate of access line installations from 1,604 in the fourth quarter of 1996 to 19,187 in the fourth quarter of 1997. Approximately 32% of the increase in total quarterly installations was driven by an increase in quarterly installations in those markets launched in 1996, where installations increased from 1,604 in the fourth quarter 1996 to 7,293 in the fourth quarter of 1997.

NEXTLINK believes that a critical factor in the successful implementation of its strategy is the quality of its management team and their extensive experience in the telecommunications industry. The Company has built a management team that it believes is well suited to challenge the dominance of the ILECs in the local exchange market. Craig O. McCaw, the Company's founder and largest and controlling shareholder, Steven W. Hooper, the Company's Chairman of the Board, Wayne M. Perry, the Company's Vice Chairman and Chief Executive Officer, James F. Voelker, the Company's President, and George M. Tronsrue III, the Company's Chief Operating Officer, each has 15 or more years of experience in leading companies in competitive segments of the telecommunications industry. In addition, the presidents of the Company's operating subsidiaries and the Company's senior officers have an average of 14 years of experience in the telecommunications industry. Mr. Hooper and Mr. Perry were members of the senior management team at McCaw Cellular Communications, Inc. ("McCaw Cellular") during the years in which it became the nation's largest cellular telephone company. Following McCaw Cellular's sale to AT&T Corp. in 1994, Messrs. Perry and Hooper were Vice Chairman and Chief Executive Officer, respectively, of AT&T Wireless Services, Inc.

Market Opportunity

Prior to 1984, AT&T Corp. ("AT&T") dominated both the local exchange and long distance marketplace by owning the operating entities that provided both local exchange and long distance services to most of the U.S. population. While long distance competition began to emerge in the late 1970s, the critical event triggering the growth of long distance competition was the breakup of AT&T and the separation of its local and long distance businesses as mandated by the Modified Final Judgment relating to the breakup of AT&T (the "MFJ"). To foster competition in the long distance market, the MFJ prohibited AT&T's divested local exchange businesses, the Regional Bell Operating Companies ("RBOCs"), from acting as a single source provider of telecommunications services.

The Company believes that a similarly critical event occurred in 1996 with the passage of the Telecom Act. In most locations throughout the United States, the ILEC has operated with a virtual monopoly over the provision of most local exchange services. However, just as competition slowly emerged in the long distance business prior to the MFJ, competitive opportunities also have slowly emerged over the last 10 years at the local level.

Industry sources estimate that in 1996 the total revenues from local and long distance telecommunications services were approximately $183 billion, of which approximately $101 billion were derived from local exchange services and approximately $82 billion from interLATA long distance services. Based upon FCC information, aggregate revenues for local and long distance services grew at a compounded annual rate of approximately 5.5% between 1991 and 1996. Although the MFJ relating to the breakup of AT&T established the preconditions for competition in the market for long distance services in 1984, the market for local exchange services has been, until recently, virtually closed to competition and has largely been dominated by regulated monopolies. Efforts to open the local exchange market began in the late 1980s on a state-by-state basis when competitive access providers ("CAPs") began offering dedicated private line transmission and special access services. These types of services together currently account for approximately 12% of the total local exchange revenues. CAPs were restricted, often by state laws, from providing the other, more frequently used services such as basic and switched services, which today account for approximately 88% of local exchange revenues.

The Telecom Act and the FCC's issuance of rules for competition, particularly those requiring the interconnection of all networks and the interchange of traffic among the ILECs and the CLECs, as well as pro-competitive policies already developed by state regulatory commissions, have caused fundamental changes in the structure of the local exchange markets. Although a recent decision by the United States Court of Appeals for the Eighth Circuit substantially limits the FCC's jurisdiction and expands the state regulators' jurisdiction to set and enforce rules governing the development of local competition, most states have already begun to establish rules for local competition that are consistent with the FCC rules overturned by the Eighth Circuit. See "— Regulatory Overview."

These developments create opportunities for new entrants offering local exchange services to capture a portion of the ILEC's dominant, and historically monopoly controlled, market share of local services. The development of switched local services competition, however, is in its early stages and the Company believes that CLECs currently serve fewer than 5% of the total business lines in the United States.

NEXTLINK believes that the provisions of the Telecom Act requiring the ILECs to cooperate on a technical level with competitors are as significant as the Telecom Act's provisions eliminating state laws barring competitors from entering the local exchange services market. Under the Telecom Act, the FCC and state regulators are required to ensure that ILECs implement:

- Interconnection — provides competitors the right to connect to the ILECs' networks at any technically feasible point and to obtain access to its rights-of-way;

- Unbundling of the Local Network — allows competitors to purchase and utilize components of the ILECs' network selectively;

- Reciprocal Compensation — establishes the framework for pricing between the CLEC and the ILEC for use of each other's networks; and

- Number Portability — allows ILEC customers to retain their current telephone numbers when they switch to a CLEC.

In addition, the Telecom Act provides that ILECs that are subsidiaries of RBOCs cannot combine in-region, long distance services across local access and transport areas ("LATAs") with the local services they offer until they have demonstrated that they have complied with certain regulatory requirements relating to local competition. See "— Regulatory Overview." One federal district court has ruled that the Telecom Act's restrictions on RBOC long distance entry are unconstitutional. This decision has been stayed pending appeal. See " — Federal legislation." The Company believes it will have an opportunity to gain market share in certain markets by combining local and long distance services in a single offering to its customers before that market's ILEC, if it is a subsidiary of a RBOC, is permitted to do so.

Business Strategy

The Company has built an end user-focused, locally oriented organization dedicated to providing switched local and long distance telephone service at competitive prices to small and medium-sized businesses. The key components of the Company's strategy to become a leading provider of competitive telecommunications services and to maximize penetration of its targeted customer base are:

Provide Integrated Telecommunications Services to Small and Medium-Sized Businesses. The Company primarily focuses its sales efforts for switched local and long distance services on small and medium-sized businesses and professional groups, those businesses having fewer than 50 business lines. The Company's market research indicates that these customers prefer a single source for all of their telecommunications requirements, including products, billing, installation, maintenance and customer service. The Company has chosen to focus on this segment based on its expectations that higher gross margins will generally be available on services provided to these customers as compared with larger business, and that ILECs may be less likely to apply significant resources towards retaining these customers. The Company expects to attract and retain these customers through a direct sales effort by offering: (i) bundled local and long distance services, as well as the Company's enhance communications services; (ii) up to a 10% to 15% discount to comparable pricing by the ILEC as well as promotional discounts, depending on the individual market; and (iii) responsive customer service and account management provided on a local level.

Foster Decentralized Local Management and Control. The Company believes that its success is enhanced by building locally based management teams that are responsible for the Company's success in each of their operational markets. The Company has recruited experienced entrepreneurs and industry executives as presidents of each of the Company's operating subsidiaries, many of whom have previously built and led their own start-up telecommunications businesses. The local presidents and their teams are charged with achieving growth objectives in their respective markets and have decision making authority in key operating areas, including customer care, network growth and building connectivity, and managing the relationship and provisioning efforts with the ILEC. The Company has established an incentive based compensation policy for these management teams that is based upon the achievement of targeted growth and operational objectives. The Company believes that this local management focus will provide a critical competitive edge in customer acquisition and retention in each market.

Further Develop Effective Direct Sales and Customer Care Organizations. NEXTLINK is building a highly motivated and experienced direct sales force and customer care organization that is designed to establish a direct and personal relationship with its customers. The Company has expanded its sales force from 98 salespeople at year end 1996 to 223 salespeople at December 31, 1997. The Company expects to further increase its sales force to approximately 350 salespeople by year end 1998. Salespeople are given incentives through a commission structure that targets 40% of a salesperson's compensation to be based on performance. To ensure customer satisfaction, each customer will have a single point of contact for customer care who is responsible for solving problems and responding to customer inquiries. The Company has expanded its customer care organization from 36 customer care employees at year end 1996 to 162 customer care employees at December 31, 1997. The Company expects to further increase its customer care organization to approximately 275 customer care employees by year end 1998.

Continuously Improve Provisioning Processes to Accelerate Revenue Growth. The Company believes that a significant ongoing challenge for CLECs will be to continuously improve provisioning systems, which include the complex process of transitioning ILEC customers to the Company's network. Accordingly, the Company will continue to identify and focus, as a key competitive strategy, on implementing best provisioning practices in each of its markets that will provide for rapid and seamless transitions of customers from the ILEC to the Company. To support the provisioning of its services, the Company has begun the long-term development and implementation of a comprehensive information technology platform geared toward delivering information and automated ordering and provisioning capability directly to the end user as well as to the Company's internal staff. The Company believes that these practices and its comprehensive information technology platform, as developed, will provide the Company with a long-term competitive advantage and allow it to more rapidly implement switched local services in its markets and to shorten the time between the receipt of a customer order and the generation of revenues. The Company's improving capacity to provision access lines to its networks is reflected in the number of access lines installed per business day. For those markets in which the Company has offered switched local services since 1996, the rate increased from 44 installations per business day in the first quarter of 1997 to 309 per business day in the fourth quarter of 1997.

Develop High Capacity Fiber Optic Networks with Broad Market Coverage. NEXTLINK designs its networks with a long-term view focusing on three key elements. First, the Company designs and builds its networks to provide extensive coverage of those areas where the density of business lines is highest and to enable the Company to provide direct connections to a high percentage of nearby commercial buildings and ILEC central offices situated near the network. Over time, this broad coverage is expected to result in a higher proportion of traffic that is both originated and terminated on the Company's networks, which should provide higher long-term operating margins. In addition, the Company is participating in the FCC's Local Multipoint Distribution Service ("LMDS") auction which, depending on the bidding and deployment costs, may offer an economically efficient means to supplement the Company's fiber network build-out in some localities. Furthermore, a wireless local loop alternative may create competitive pressure on high unbundled loop costs in certain areas. Second, the Company constructs high capacity networks that utilize large fiber bundles capable of carrying high volumes of voice, data, video and Internet traffic as well as other high bandwidth services. This strategy should reduce potential "overbuild" costs and provide added network capacity as the Company adds high bandwidth services in the future. In Atlanta, Chicago, New York and Newark, New Jersey, the Company will utilize leased dark fiber and fiber capacity to launch facilities-based services and begin building a customer base in advance of completing construction of its own fiber optic network in these markets. Third, the Company employs a uniform technology platform based on Nortel DMS 500 switches, associated distribution technology and other common transmission technologies enabling the Company to (i) deploy features and functions quickly in all of its networks, (ii) expand switching capacity in a cost effective manner and (iii) lower maintenance costs through reduced training and spare parts requirements. The Company currently has 12 operational Nortel DMS 500 switches, including one installed switch at the Company's testing and network operations control center ("NEXTLAB"). For economic or strategic reasons, the Company may in the future elect to utilize other switch vendors and may also acquire and utilize non-Nortel switches in connection with acquisitions of other companies. The Company plans to install three additional Nortel DMS 500 switches by June 1998. The Company also utilizes unbundled loops from the ILEC to connect the Company's switch and network to end user buildings and is evaluating other alternatives for building connectivity, including wireless connections, for the "last mile" of transport.

Continue Market Expansion. The Company's goal is to add markets and market clusters to increase its addressable business lines to approximately 15 million by the end of 1998 and 21 million by the end of 1999. The Company anticipates continued expansion into new geographic areas, including additional large markets, as opportunities arise either through building new networks, acquiring existing networks or other telecommunications companies, or acquiring or leasing dark fiber and fiber capacity. NEXTLINK also believes that its strategy of operating its networks in clusters (i) offers substantial advantages including economies of scale in management, marketing, sales and network operations, (ii) enables the Company to capture a greater percentage of regional traffic and to develop regional pricing plans, because the Company believes that a significant level of traffic terminates within 300 miles of its origination and (iii) provides opportunities in smaller markets that are too small to develop on a stand-alone basis.

Offer Enhanced Communications Services. NEXTLINK offers customers value-added services such as the Company's IVR products that are not dependent on the Company's local facilities. The Company offers its enhanced communications services in all of its markets, as well as in areas of planned network expansion. The Company believes these services increase its visibility in attracting local exchange customers when it operates networks in these markets.

The Company's Telecommunications Services

Local and Long Distance Services

The Company commenced the offering of switched local and long distance services in seven markets on July 4, 1996, and in 18 additional markets in 1997. In February 1998, the Company launched switched local and long distance services in Chicago, Illinois and expects to commence the offering of switched local and long distance services in additional markets, including the south San Francisco Bay Area, New York City, Atlanta and Newark (NJ) areas, during the remainder of 1998. The Company focuses its product offering on basic telecommunications services, which it believes are the core of local exchange services. Pricing, which is determined and implemented by the Company's operating subsidiary in each local market, has been generally 10% to 15% lower than the pricing for comparable local services from the ILEC and the Company also makes promotional offering prices available from time to time. The Company's current product offering includes:

- Standard dial tone, including touch tone dialing, 911, and operator assisted calling;
- Multi-trunk services, including direct inward dialing (DID) and direct outward dialing (DOD);
- Long distance service, including 1+, 800/888 and operator services;
- Voice messaging with personalized greetings, send, transfer, reply and remote retrieval capabilities; and
- Directory listings and assistance.

Currently, the Company offers CAP services in 26 markets, focusing on long distance carriers and the private line needs of high volume customers. In addition, data services that are currently offered by the Company include Ethernet, TOKEN rings, and Fiber Distributed Data Interface (FDDI).

The Company's CAP services, which are used as both primary and back-up circuits, fall into three principal categories: (1) special access circuits that connect end users to long distance carriers, (2) special access circuits that connect long distance carriers' facilities to one another and (3) private line circuits that connect several facilities owned by the same end user.

Enhanced Communications Services

NEXTLINK's IVR platform allows a consumer to dial into a computer-based system using a toll-free number and a touch tone phone and, by following a customized menu, to access a variety of information and to leave, simultaneously, a profile of the caller behind for use by either NEXTLINK or its clients. Currently, NEXTLINK provides four types of IVR services:

- *LeaveWord* — prompts the consumer to leave messages of any length or complexity, ranging from catalog requests and contest entries to specific product questions and surveys;
- *Dealer Locator* — helps a consumer to locate the nearest dealer of the client's products by instantly identifying the consumer's area and responding with the names, addresses and phone numbers of the client's locations within any desired mileage radius;
- *Automated Order Entry* — allows consumers to purchase products using the interactive phone service 24-hours a day, with real-time order and credit card confirmation as well as arranging for delivery of the new item to the consumer's desired address; and
- *Interactive Call Center* — provides the consumer with a menu of selections that include Dealer Locator, Automated Order Entry and other functions, including receiving a catalog, registering the warranty of a product, contest entry and an option for callers to be forwarded to a live operator.

The Company anticipates that it will continue to explore other enhanced communications services opportunities and may acquire, invest in or establish marketing relationships with additional service providers in the future that support its overall business and marketing strategies.

Sales and Customer Care

Overview

The Company utilizes a two-pronged sales strategy in each of its markets, one directed to the sale of local and long distance services and the other to enhanced communications services. The primary sales efforts in the Company's markets are for switched local and long distance services focusing on small and medium-sized businesses and professional groups with fewer than 50 business lines. The Company's market research indicates that these customers prefer a single source for all of their telecommunications requirements, including products, billing, installation, maintenance and customer service. The Company utilizes a direct sales effort offering combined local and long distance services with prices that are generally at a 10% to 15% discount from the ILEC. Providing a combination of local and long distance services provides the Company's customers a level of convenience that has been generally unavailable since the break-up of AT&T. The Company is also marketing its enhanced communications services through a separate direct sales force in each market, which is expected to increase the number of customers for all of NEXTLINK's telecommunications services in that market at a faster rate. In addition, the Company is continuing its sales efforts for traditional CAP services to long distance carriers and large commercial users.

Sales Force

The Company is building a highly motivated and experienced direct sales force and customer care organization that is designed to establish a direct and personal relationship with its customers. The Company seeks to recruit salespeople with strong sales backgrounds, including salespeople from long distance companies, telecommunications equipment manufacturers, network systems integrators and the ILECs. The Company has expanded its sales force from 98 salespeople at year end 1996 to 223 salespeople at December 31, 1997. The Company expects to further increase its sales force to approximately 350 salespeople by year end 1998. Salespeople are given incentives through a commission structure that targets 40% of a salesperson's compensation to be based on performance. With respect to traditional CAP services, the Company currently utilizes a national sales force to establish and expand long distance company access service sales. Sales efforts for long distance carriers are centralized in order to provide a single point of contact for these customers.

The Company anticipates that its enhanced communications service offerings will continue to be sold across the country by its existing national sales force for these services. The Company has also augmented these efforts with a separate, targeted, locally based sales force in each of its markets. The Company believes that this approach to each market will provide revenues that are incremental to its local exchange operations.

Customer Care

The Company is augmenting its direct sales approach with superior customer care and support through locally based customer care representatives. The Company is structuring its customer care organization in such a manner that each customer will have a single point of contact for customer care who is responsible for solving problems and responding to customer inquiries. The Company has expanded its customer care organization from 36 customer care employees at year end 1996 to 162 customer care employees at December 31, 1997. The Company seeks to provide a customer care group that has the ability and resources to respond to and resolve customer problems as they arise. The Company believes that customer care representatives will be the most effective if they are based in the community in which the Company is offering services, which placement will allow, among other things, the opportunity for the representatives to visit the customer's location.

Network Development

General

In developing its networks, the Company has generally executed a strategy of (i) acquiring fully or partially constructed fiber optic networks and (ii) designing and constructing high capacity fiber optic networks with broad coverage. The Company has recently entered into leased dark fiber and fiber capacity arrangements which allow the Company, by installing one or more switches and related electronics, to enter a market prior to completing construction of a fiber optic network. The Company regularly evaluates markets as locations for expansion of the Company's current networks and the development of additional networks. The decision to build, acquire or utilize capacity of an existing network is not based on any single factor, but on a combination of a number of factors including:

- demographic, economic, telecommunications demand and business line characteristics of the market and the surrounding markets;
- level of capital expenditures relative to the number of business lines;
- availability of rights-of-way;
- actual and potential competitors; and
- potential for the Company to cluster additional networks in the region.

If a particular market targeted for development is deemed to present an attractive market opportunity, the Company determines whether acquisition opportunities are available. In some cases a large network can be acquired, and in other cases a small existing network can serve as a starting point for market entry. If the Company decides to build a new network, or substantially expand a small acquired system, the Company designs a proposed new or expanded network that can connect a large number of businesses, long distance carriers points of presence and the ILEC's principal central offices in the area to be served, utilizing existing rights-of-way and/or rights-of-way that the Company will develop. Concurrently, the Company's market development personnel visit the location of the proposed network to begin discussions with city officials, providers of rights-of-way, potential end users and long distance companies.

Based on the data developed during these preliminary studies and visits, the Company develops detailed financial estimates of the costs of constructing a network, including the cost of fiber optic cable, transmission and other electronic equipment, as well as costs related to switching, engineering, building entrance requirements and right-of-way acquisitions. If the financial estimates are satisfactory to the Company, the Company's market development personnel prepare a detailed business and financial plan for the proposed network, including competitive, regulatory and right-of-way analyses. Based upon its review of these analyses, the Company determines whether to proceed. The Company anticipates continuing the expansion of its networks into new markets utilizing the market development analysis described above. The Company will seek to continue to expand its operations in states where it has established one or more networks, by continuing to construct or acquire networks in adjacent areas to leverage its existing networks, switches and telecommunications equipment, thereby establishing a cost effective and operationally efficient cluster of networks in various geographic regions.

The Company's Networks

The following table provides information on the markets in which the Company has launched switched local and long distance services.

State	Market	Launch Date for Switched Local Services
Tennessee	Memphis	July 1996
	Nashville	July 1996
Pennsylvania	Allentown	July 1996
	Harrisburg	July 1996
	Lancaster	July 1996
	Reading	July 1996
	Philadelphia	July 1997
	Scranton/Wilkes Barre	December 1997
Washington	Spokane	July 1996
Utah	Salt Lake City	January 1997
	Orem/Provo	September 1997
Nevada	Las Vegas	April 1997
Ohio	Cleveland	April 1997
	Columbus	April 1997
California	Anaheim	July 1997
	Costa Mesa	July 1997
	Fullerton	July 1997
	Garden Grove	July 1997
	Huntington Beach	July 1997
	Inglewood	July 1997
	Irvine	July 1997
	Long Beach	July 1997
	Los Angeles	July 1997
	Orange	July 1997
	Santa Ana	July 1997
Illinois	Chicago	February 1998

Network Architecture

Design

The Company builds or acquires its own fiber optic networks because it believes that facilities-based full service telecommunications companies whose networks are directly connected to their customers will have the ability to respond more quickly to customer needs for capacity and services. Moreover, the Company believes that facilities-based carriers develop a more knowledgeable, cooperative relationship with their customers, improving their ability to provide new services and other telecommunications solutions, which should result in higher long-term operating margins.

The Company believes that the future telecommunications market will be an interconnected network of networks. The Company believes that calls will flow between local networks, with customers selecting their service provider based on high quality and differentiated products, responsive customer service and price. In some circumstances, depending in part upon regulatory conditions, the Company will utilize its own network for one portion of a call and resell the services of another carrier for the remaining portion of a call. In other instances, both the origination and termination of calls will take place on the Company's networks. The Company's networks are designed to maximize connectivity directly with significant numbers of business end users, and to easily interconnect and provide a least-cost routing flow of traffic between the Company's network and other networks in the marketplace.

In general, the Company seeks to build wide, expansive networks, rather than a simple core ring in a downtown metropolitan area. The Company believes that this type of broad coverage of the markets in which it operates will result in the following advantages:

- an increased number of buildings that can be directly connected to the Company's network, which should maximize the number of businesses to which the Company can offer its services;
- a higher volume of telecommunications traffic both originating and terminating on the Company's network, which should result in improved operating margins;
- the ability to leverage its investment in high capacity switching equipment and electronics; and
- the opportunity for the Company's network to provide backhaul carriage for other telecommunications service providers such as long distance and wireless carriers.

The Company seeks to further utilize this network design to increase the number of buildings and customers directly connected to its networks. The Company believes that as compared to the extensive use of unbundled loops and pursuing a pure resale business strategy, having a direct connection to its customers will provide the Company with the highest long-term operating margins, allow the Company to provide greater feature and quality control as well as offer customer service that is both prompt and effective, because the network to be serviced is controlled by the Company and not another service provider.

The Company seeks to build high capacity networks using a backbone density ranging between 72 and 240 strands. A single pair of glass fibers on the Company's networks can currently transmit 32,256 simultaneous voice conversations, whereas a typical pair of copper wires can currently carry a maximum of 24 digitized simultaneous voice conversations. The Company believes that installing high count fiber strands will allow the Company to offer a higher volume of voice and broadband services without incurring significant additional construction costs.

Construction

The construction period of a new network varies depending upon the scope of the activities, such as the number of backbone route miles to be installed, whether the construction is underground or aerial, whether the conduit is in place or requires construction, the initial number of buildings targeted for connection to the network backbone and the general configuration for its deployment. After installing the network backbone, the Company evaluates extensions to additional buildings and expansions to other areas of a market, based on detailed assessments of market potential.

The Company's network backbones are installed in conduits that are either owned by the Company or leased from third parties. The Company leases conduit or pole space from entities such as utilities, railroads, long distance carriers, state highway authorities, local governments and transit authorities. These arrangements are generally for multi-year terms with renewal options, and are nonexclusive. The availability of these arrangements is an important part of the Company's evaluation of a market. Cancellation of any of the Company's material right-of-way agreements could have an adverse effect on the Company's business in that area and could have a material adverse effect on the Company.

Office buildings are connected primarily by network backbone extensions to one of a number of physical rings of fiber optic cable, which originate and terminate at the Company's central node. Alternatively, the Company may access an end user's location through interconnection with the ILEC's central office. The Company is also evaluating other alternatives for building connectivity, including wireless connections, for the "last mile" of transport. Signals are generally sent through a network backbone to the central node simultaneously on both primary and alternate protection paths. Most buildings served have a discrete Company presence (referred to as a "remote hub") located in the building. Within each building, Company-owned internal wiring connects the remote hub to the customer premise. Customer equipment is connected to Company-provided electronic equipment generally located in the remote hub, where customer transmissions are digitized, combined and converted to an optical signal. The traffic is then transmitted through the network backbone to the Company's central node where originating traffic is reconfigured for routing to its ultimate destination. After completion of network construction, the Company employs maintenance and line crews that are responsible for responding to outages and routine maintenance of the network.

In January 1998, the Company and Nextel Communications, Inc. ("Nextel") formed NEXTBAND Communications, L.L.C. ("NEXTBAND"), a joint venture which is owned 50% by the Company and 50% by Nextel. On January 20, 1998, NEXTBAND filed an application with the FCC for which it paid a $50.0 million refundable deposit to participate in the LMDS auction which began on February 18, 1998. Of the deposit amount, $25.0 million was contributed by the Company. LMDS is a fixed broadband point-to-multipoint service which the FCC and industry analysts anticipate will be used for the deployment of wireless local loop, high-speed data transfer and video broadcasting services. Two licenses will be offered in each of 493 BTAs when the auction commences. Although the number of licenses that may be awarded to NEXTBAND is limited by the amount of the deposit, NEXTBAND has applied for and is eligible to bid on any of the markets being auctioned for the block A license (1,150 MHz of spectrum) and the block B license (150 MHz of spectrum).

The Company is exploring LMDS for two reasons. Depending upon the bidding and deployment costs, LMDS may offer an economically efficient means to supplement the Company's fiber network build-out in some localities. In addition, a wireless local loop alternative may create competitive pressure on high unbundled loop costs in certain areas. There can be no assurance that NEXTBAND's participation in the auction will result in the purchase of any LMDS licenses or that LMDS spectrum for wireless connectivity will provide a cost-effective and efficiently engineered means to connect to end user locations.

In June 1997, the Company entered into an eight year exclusive agreement, which contains a five year renewal option, with a company that has excess fiber capacity in each of Atlanta, Chicago, New York and Newark (NJ). In addition to this capacity arrangement, the Company also entered into a 20-year lease of capacity over an existing 47-mile fiber network which extends from the Wall Street area north to midtown Manhattan. In February 1998, the Company entered into an agreement for exclusive rights to multiple fibers and innerducts for 20 years, with two 10 year renewals. The route covered by the agreement extends over 650 route miles from Manhattan to White Plains (NY), to Stamford (CT), to Newark (NJ) and south from Manhattan through Philadelphia, Wilmington (DE), Baltimore, and to Washington (DC). The route will offer frequent splice points within metropolitan areas and splice points at least every 10,000 feet on routes between metropolitan areas, as well as provide access to ILEC central and tandem switching offices.

Uniform Technology Platform

The Company is implementing a consistent technology platform based on the Nortel DMS 500 switch throughout its networks. Unlike a traditional long distance or local switch, the Nortel DMS 500 switch will enable the Company to provide local and long distance services from a single platform. The Company believes that having a standardized switch platform will enable it to (i) deploy features and functions quickly in all of its networks, (ii) expand switch capacity in a cost effective manner and (iii) lower maintenance costs through reduced training and spare parts requirements. In addition, the scalability and capacity of these switches will allow the Company to switch calls from more than one market, which enhances the Company's ability to use a clustered approach to the building of its networks. For economic or strategic reasons, the Company may in the future elect to utilize other switch vendors and may also acquire and utilize non-Nortel switches in connection with acquisitions of other companies.

The Company also is establishing a uniform transmission technology utilizing SONET design and standardized digital access and cross connect systems ("DACCS") and other ancillary transmission equipment. DACCS provide the ability to aggregate and disaggregate capacity along the fiber optic network. Using DACCS, the capacity of 24 DS-0s can be aggregated to form a DS-1 and, again through the DACCS, 28 DS-1s can be aggregated to form a DS-3.

The Company's NEXTLAB facility contains a fully functional Nortel DMS 500 switch in a configuration that simulates the working environment of the Company's operational switches as well as distribution and ancillary equipment. Located in Plano, Texas, NEXTLAB operates separate and apart from the Company's operational switches as a testing facility and will serve as the Company's network operations control center

(NOCC). NEXTLAB provides the Company with a means to test switch software and service configurations prior to their release on the Company's networks. The Company believes that this process should: (i) minimize network outages, (ii) save network operating and training costs and (iii) improve levels of customer service.

Implementation of Local Telecommunications

A company preparing to offer local exchange services not only requires an installed switch, but also must have numerous network and routing arrangements in place. NEXTLINK has established all of these arrangements for Pennsylvania, Tennessee, Washington, Utah, Ohio, Nevada, California and Illinois. These key elements include:

Interconnection. The Company has executed interconnection agreements for all of its current operating networks: in Nashville and Memphis, Tennessee, with BellSouth Telecommunications, Inc.; in Harrisburg, Reading, Lancaster and Allentown, Pennsylvania, with Bell Atlantic-Pennsylvania, Inc.; in New York, New York with Bell Atlantic-New York, Inc.; in Chicago, Illinois, and in Cleveland and Columbus, Ohio, with a division of Ameritech; in Spokane, Washington, and Salt Lake City and Provo/Orem, Utah with U S WEST Communications, Inc.; in Los Angeles, California and the surrounding markets, with Pacific Bell and GTE Corporation; and in Las Vegas, Nevada, with a division of Sprint. The Company is currently negotiating with BellSouth for an interconnection agreement to cover Atlanta by the end of the third quarter of 1998. In addition, the Company believes that interconnection arrangements between the ILECs and other CLECs or the Company will be in place in other markets that the Company may enter. The Company likely will initially "piggy-back" on these other arrangements while pursuing more favorable long-term arrangements.

The Company's approach to interconnection has been a two-step process. To accelerate its launch of switched local services, the Company has entered into initial interconnection arrangements that allow for the immediate exchange of local traffic with the ILEC. These arrangements allow the Company to commence service immediately and then work to optimize its arrangements with the ILEC. The Company's ILEC agreements are now being re-negotiated under Sections 251 and 252 of the Telecom Act. The actual operating experience gained through the Company's initial interconnection agreements gives the Company critical knowledge for negotiating longer term arrangements. In some cases, where agreement on a long-term arrangement cannot be reached, the Company may pursue binding arbitration before the state utility commissions as provided under the Telecom Act. The Company currently has arbitration proceedings pending in Pennsylvania and Tennessee with Bell Atlantic and BellSouth, respectively. Negotiations are continuing with both parties during the pendency of the arbitration proceedings. There can be no assurance, however, that the Company will be able to negotiate longer term relationships on terms and conditions satisfactory to the Company.

Telephone Numbers. The Company has been offered interim number portability arrangements by the ILEC in each of its markets, and the Company also is engaged in industry negotiations to establish permanent number portability. Number portability arrangements will allow ILEC customers to retain their telephone numbers when changing local exchange service carriers. In addition, the Company has been allocated multiple blocks of 10,000 telephone numbers for each of its Tennessee, Washington, Pennsylvania, Ohio, Utah, Nevada, California and Illinois networks, and has applied for such numbers in New York, for use in assigning new numbers to its customers. These numbers, known as NXX numbers, are the first three digits of a customer's seven digit local phone number. In each of these cases, the NXX is fully loaded into the Local Exchange Routing Guide or LERG, which instructs ILECs and other carriers to send a call using a NEXTLINK NXX to the appropriate NEXTLINK switch, for delivery to the NEXTLINK customer.

SS7 Point Codes. For each of the Company's switches, the Company has been assigned Point Codes for use with the advanced signaling system known as SS7 which is a separate or "out of band" communications channel used between telecommunications carriers to set up and control traffic on and between networks. The Company has designed its network to fully utilize SS7 signaling, which improves call processing times and frees capacity for voice, data, and video transmissions. The Company has entered into an agreement with a national SS7 service provider that will allow the Company to utilize SS7 signaling in its current and new markets nationwide.

Regulatory Overview

Overview

The Company's services are subject to varying degrees of federal, state and local regulation. The FCC generally exercises jurisdiction over the facilities of, and services offered by, telecommunications common carriers that provide interstate or international communications. The state regulatory commissions retain jurisdiction over the same facilities and services to the extent they are used to provide intrastate communications. Local governments sometimes impose franchise or licensing requirements on local exchange and other carriers and regulate street opening and construction activities.

The Telecom Act imposes on ILECs certain interconnection obligations that, taken together, grant competitive entrants such as the Company what is commonly referred to as "co-carrier status." In addition, the Telecom Act generally preempts state or local legal requirements that prohibit or have the effect of prohibiting any entity from providing telecommunications services. The Telecom Act allows state regulatory authorities to continue to impose competitively neutral requirements designed to promote universal service, protect public safety and welfare, maintain quality of service and safeguard the rights of consumers. The Telecom Act also preserves the ability of state and local authorities to manage and require compensation for the use of public rights-of-way by telecommunications providers including competitors of the ILECs in the local market.

It is anticipated that co-carrier status and the preemption of state and local prohibitions on entry could permit the Company to become a full service provider of switched telecommunications services anywhere in the United States. The following table summarizes the interconnection rights granted by the Telecom Act that are most important to the achievement of this goal and the Company's belief as to the anticipated effect of the new requirements, if properly implemented.

Issue	Definition	Anticipated Effect
Interconnection	Efficient network interconnection to transfer calls back and forth between ILECs and competitive networks (including 911, 0+, directory assistance, etc.)	Allows a CLEC to service and terminate calls to and from customers connected to other networks
Local Loop Unbundling	Allows competitors to selectively gain access to ILEC wires which connect ILEC central offices with customer premises	Reduces the capital costs of a CLEC to serve customers not directly connected to its networks
Reciprocal Compensation	Mandates reciprocal compensation for local traffic exchange between ILECs and competitors	Improves the CLEC's margins for local service
Number Portability	Allows customers to change local carriers without changing numbers; true portability allows incoming calls to be routed directly to a competitor. Interim portability allows incoming calls to be routed through the ILEC to a competitor at the economic equivalent of true portability	Allows customers to switch to a CLEC's local service without changing phone numbers
Access to Phone Numbers	Mandates assignment of new telephone numbers to competitive telecommunications provider's customers	Allows CLECs to provide telephone numbers to new customers on the same basis as the ILEC

While the interconnection rights established in the Telecom Act are a necessary prerequisite to the introduction of full local competition, they must be properly implemented to be effective. Significant implementation issues remain to be resolved, including modifications to, and expansions of, the ILEC network interface facilities, before the barriers to entry into the local telephone business are sufficiently lowered to permit widespread competitive entry. See "Federal Legislation" below for a more complete explanation of the potential effect of the Telecom Act on the Company's business.

Federal Legislation

The Telecom Act, enacted on February 8, 1996, substantially revised the Communications Act of 1934. The Telecom Act establishes a regulatory framework for the introduction of local competition throughout the United States. Among other things, the Telecom Act preempts any state or local government from prohibiting any entity from providing telecommunications service. This provision eliminated prohibitions on entry found in almost half of the states in the country at the time the Telecom Act was passed. In addition, the Telecom Act now requires that ILECs provide CLECs with physical collocation on rates, terms and conditions that are just and reasonable, unless the ILEC can demonstrate to state regulators that physical collocation is not practical. The Company believes that either physical or virtual collocation of its facilities in a timely fashion for appropriate rates and terms will accommodate its purposes.

The Telecom Act also establishes a dual federal-state regulatory scheme for eliminating other barriers to competition faced by competitors to the ILECs and other new entrants into the local telephone market. Specifically, the Telecom Act imposes on ILECs certain interconnection obligations, some of which are to be implemented by FCC regulations. The Telecom Act contemplates that states will apply the federal regulations and oversee the implementation of all of the aspects of interconnection not subject to FCC jurisdiction as they oversee interconnection negotiations between ILECs and their new competitors.

In addition, the Telecom Act provides that ILECs that are subsidiaries of RBOCs cannot combine in-region long distance services across LATAs with the local services they offer until they have demonstrated that (i) they have entered into an approved interconnection agreement with a facilities-based CLEC or that no such CLEC has requested interconnection as of a statutorily determined deadline, (ii) they have satisfied a 14-element checklist designed to ensure that the ILEC is offering access and interconnection to all local exchange carriers on competitive terms and (iii) the FCC has determined that in-region, interLATA approval is consistent with the public interest, convenience and necessity.

On July 2, 1997, SBC and its local exchange carrier subsidiaries filed a lawsuit in the United States District Court for the Northern District of Texas challenging on Constitutional grounds the Telecom Act restrictions applicable to the RBOCs only. On December 31, 1997, the District Court ruled in favor of SBC and held that Sections 271 through 275 of the Telecom Act, including the long distance entry provisions, are unconstitutional. On February 11, 1998, however, the District Court issued a stay of its December 31, 1997 decision pending appeal to the United States Circuit Court of Appeals for the Fifth Circuit. The appeal is currently pending.

Federal Regulation

The FCC has significant responsibility in the manner in which the Telecom Act will be implemented especially in the areas of universal service, access charges, numbering, number portability and price caps. The details of the rules adopted by the FCC will have a significant effect in determining the extent to which barriers to competition in local services are removed, as well as the time frame within which such barriers are eliminated. The FCC may also grant ILECs increased pricing flexibility to enable them to respond to competition for special access and private line services. To the extent such pricing flexibility is granted, the Company's ability to compete for certain services may be adversely affected.

On August 8, 1996, the FCC issued an order containing rules providing guidance to the ILECs, CLECs, long distance companies and state PUCs regarding several provisions of the Telecom Act. The rules include, among other things, FCC guidance on (i) discounts for end-to-end resale of ILEC local exchange services (which the FCC has suggested should be in the range of 17%-25%), (ii) availability of unbundled local loops and other unbundled ILEC network elements, (iii) the use of Total Element Long Run Incremental Costs ("TELRIC") in the pricing of these unbundled network elements, (iv) average default proxy prices for unbundled local loops in each state, (v) mutual compensation proxy rates for termination of ILEC/CLEC local calls and (vi) the ability of CLECs and other interconnectors to opt into portions of interconnection agreements negotiated by the ILECs with other parties on a most favored nation (or a "pick and choose") basis. See below for a discussion of the Eighth Circuit Court of Appeals decision invalidating certain aspects of this order.

On May 8, 1997, the FCC released an order establishing a significantly expanded federal telecommunications subsidy regime. For example, the FCC established new subsidies for services provided to qualifying schools and libraries with an annual cap of $2.25 billion and for services provided to rural health care providers with an annual cap of $400 million. The FCC also expanded the federal subsidies to low income consumers. Providers of interstate telecommunications services, such as the Company, as well as certain other entities, must pay for these programs. The Company's share of the schools, libraries and rural health care funds will be based on its share of the total industry telecommunications service and certain defined telecommunications end user revenues. The Company's share of all other federal subsidy funds will be based on its share of the total interstate telecommunications service and certain defined telecommunications end user revenues. The Company intends to make all subsidy payments required by law. In the May 8 order, the FCC also announced that it will soon revise its rules for subsidizing service provided to consumers in high cost areas. Several parties have appealed the May 8 order. Such appeals have been consolidated and transferred to the United States Court of Appeals for the Fifth Circuit where they are currently pending. In addition, on July 3, 1997, several ILECs filed a petition for stay of the May 8 order with the FCC. That petition is also pending.

In a combined Report and Order and Notice of Proposed Rulemaking released on December 24, 1996, the FCC made changes and proposed further changes in the interstate access charge structure. In the Report and Order, the FCC removed restrictions on ILECs' ability to lower access prices and relaxed the regulation of new switched access services in those markets where there are other providers of access services. If this increased pricing flexibility is not effectively monitored by federal regulators, it could have a material adverse effect on the Company's ability to compete in providing interstate access services. On May 16, 1997, the FCC released an order revising its access charge rate structure. The new rules substantially increase the costs that ILECs subject to the FCC's price cap rules ("price cap LECs") recover through monthly, no-traffic sensitive access charges and substantially decrease the costs that price cap LECs recover through traffic sensitive access charges. In the May 16 order, the FCC also announced its plan to bring interstate access rate levels more in line with cost. The plan will include rules to be established sometime this year that grant price cap LECs increased pricing flexibility upon demonstrations of increased competition (or potential competition) in relevant markets. The manner in which the FCC implements this approach to lowering access charge levels will have a material effect on the Company's ability to compete in providing interstate access services. Several parties have appealed the May 16 order. Those appeals have been consolidated and transferred to the United States Court of Appeals for the Eighth Circuit where they are currently pending.

As part of its overall plan to lower interstate access rates, the FCC also released an order on May 21, 1997, in which the FCC revised its price cap rules. In the order, the FCC increased the so-called X-Factor (the percentage by which price cap LECs must lower their interstate access charges every year, net of inflation and exogenous cost increases) and made it uniform for all price cap LECs. The results of these rule changes will be both a one-time overall reduction in price cap ILEC interstate access charges and an increase in the rate at which those charges will be reduced in the future. Several parties have appealed the May 21 order. Those appeals were consolidated and transferred to the United States Court of Appeals for the Tenth Circuit. They have been subsequently transferred to the United States Court of Appeals for the District of Columbia where they are currently pending.

On January 2, 1997, Ameritech of Michigan became the first RBOC to apply for authority to provide in-region interLATA service pursuant to Section 271 of the Telecom Act. The application was withdrawn and refiled on May 21, 1997. That application was denied on August 19, 1997. In denying the application, the FCC established specific and substantial criteria that must be met before future Section 271 applications will be granted.

On April 11, 1997, SBC Communications, Inc. ("SBC") applied to the FCC for authority to provide in-region interLATA service in the state of Oklahoma. On June 26, 1997, the FCC released an order rejecting SBC's application on the grounds that SBC had not demonstrated either that SBC had entered into an approved interconnection agreement with a facilities-based CLEC or that no CLEC had requested interconnection as of the statutory deadline. On July 3, 1997, SBC filed an appeal of the June 26 order with the United States Court of Appeals for the District of Columbia. On March 20, 1998, the Court of Appeals upheld the FCC's order.

In September and November 1997, BellSouth Corporation ("BellSouth") filed applications for authorization to provide in-region interLATA service in the states of South Carolina and Louisiana. On December 24, 1997 and February 4, 1998, respectively, the FCC released orders rejecting BellSouth's applications which conclude that BellSouth had not yet demonstrated that it generally offered each of the items of the competitive checklist set forth in the Telecom Act. On January 13, 1998, BellSouth filed an appeal for the December 24, 1997 ruling with the United States District Court of Appeals for the District of Columbia. That appeal is currently pending.

The Company anticipates that RBOCs will continue to apply for authority to provide in-region interLATA services in markets where the Company operates or plans to operate. The Company also expects that the FCC will initiate a number of additional proceedings, on its own initiative and as a result of requests from CLECs and others, as a result of the Telecom Act. While the Eighth Circuit's recent decision in the appeal of the August 8, 1996 order limits the FCC's jurisdiction over the local competition provisions of the Telecom Act, such proceedings may nonetheless further define and construe the Telecom Act's terms.

Court of Appeals Decision

Various parties, including ILECs and state PUCs, filed appeals of the FCC's August 8, 1996 order in various U. S. Courts of Appeal, and several parties petitioned the FCC and the courts to stay the effectiveness of the FCC's rules included in the FCC's order, pending a ruling on the appeals. Many of the appeals were consolidated and transferred to the United States Court of Appeals for the Eighth Circuit. On July 18, 1997, the Eighth Circuit overturned the pricing rules established in the August 8, 1996 order, except those applicable to commercial mobile radio service providers. The Eighth Circuit held that, in general, the FCC does not have jurisdiction over prices for interconnection, resale, leased unbundled network elements and traffic termination. The Eighth Circuit also overturned the FCC's "pick and choose" rules as well as certain other FCC rules implementing the Telecom Act's local competition provisions. In addition, the Eighth Circuit decision substantially limits the FCC's authority to enforce the local competition provisions of the Telecom Act.

On October 14, 1997, the Eighth Circuit vacated the FCC's rule prohibiting ILECs from separating unbundled network elements that are already combined, except at the request of CLECs. In addition, under the decision, ILECs are not required to recombine unbundled network elements, but must make such elements available for CLECs to recombine on their own.

On January 22, 1998, the Eighth Circuit issued a writ of mandamus ordering the FCC to follow the court's July 1997 decision in addressing certain pricing issues in the context of RBOC Section 271 in-region interLATA entry applications.

On January 26, 1998, the United States Supreme Court agreed to hear challenges to the Eighth Circuit's July 18, 1997 and October 14, 1997 decisions. The Court has agreed to review all issues raised by the government, the RBOCs, and competitors. These include whether the FCC has authority (i) to set prices that ILECs charge CLECs for access to local networks, (ii) to require ILECs to allow CLECs to use provisions of existing interconnection agreements in their own agreements and (iii) to force ILECs to offer existing combinations of unbundled network elements needed to provide local service. Because the Court will hear the consolidated cases in its next term which begins in October, a decision is not expected until next year.

In the short term the Company believes that the Eighth Circuit decisions will not have a material adverse effect on it, because the Company already has interconnection agreements in place, or expects to have such agreements in place, under the provisions of the FCC's order and the Telecom Act which were not invalidated by the Court. The decision does not delay the implementation of the Telecom Act by the parties and by the state PUCs, but rather eliminates the guidance on pricing and most favored nation procedures as well as other issues that the FCC sought to provide to parties and the state PUCs.

In the long term, the Eighth Circuit's decisions make it more likely that the rules governing local competition will vary from state to state. Most states have already begun to establish rules for local competition that are consistent with the FCC rules overturned by the Eighth Circuit. If a patchwork of state regulations were to develop, it could increase the Company's costs of regulatory compliance and could make competitive entry in some markets more difficult and expensive than in others.

State Regulation

The Company expects that as it offers local exchange and other intrastate services in an increasing number of states, it will be subject to direct state public utility commission ("PUC") regulation in most, if not all, such states. In states where the Company desires to offer its services, the Company may be required to obtain authorization from the appropriate state commission, including certification as a CLEC. In all states where the Company is operational and certification as a CLEC is currently required, the Company's operating subsidiaries are certificated. In those markets where the Company anticipates launching services in 1998, it has received or applied for such certification.

In most states, the Company is required to file tariffs or price lists setting forth the terms, conditions and prices for services which are classified as intrastate. In some states, the Company's tariff can list a range of prices for particular services, and in others, such prices can be set on an individual customer basis. The Company is not subject to price cap or to rate of return regulation in any state in which it currently provides services.

As noted above, as a result of the July 18, 1997 Eighth Circuit decision, PUCs have an even more significant responsibility in implementing the Telecom Act. Specifically, the states have authority to establish interconnection pricing, including unbundled loop charges, reciprocal compensation and wholesale pricing. The states are also charged under the Telecom Act with overseeing the arbitration process for resolving interconnection negotiation disputes between CLECs and the ILECs. The Telecom Act allows state regulatory authorities to continue to impose competitively neutral requirements designed to promote universal service, protect public safety and welfare, maintain quality of service and safeguard the rights of consumers.

Local Government Authorization

In certain locations, the Company is required to obtain local franchises, licenses or other operating rights and street opening and construction permits to install, expand and operate its fiber-optic networks. In some of the areas where the Company provides network services, the Company's subsidiaries pay license or franchise fees based on a percentage of gross revenues or on a per linear foot basis. There is no assurance that certain cities that do not currently impose fees will not seek to impose such fees in the future, nor is there any assurance that, following the expiration of existing franchises, fees will remain at their current levels. Under the Telecom Act, state and local governments retain the right to manage the public rights-of-way and to require fair and reasonable compensation from telecommunications providers, on a competitively neutral and nondiscriminatory basis, for use of public rights-of-way.

If any of the Company's existing franchise or license agreements were terminated prior to its expiration date and the Company were forced to remove its fiber from the streets or abandon its network in place, such termination would have a material adverse effect on the Company's subsidiary in that area and could have a material adverse effect on the Company. The Company believes that the provisions of the Telecom Act barring state and local requirements that prohibit or have the effect of prohibiting any entity from providing telecommunications service should be construed to limit any such action. However, there can be no assurance that one or more local authorities will not attempt to take such action. Nor is it clear that the Company would prevail in any judicial or regulatory proceeding to resolve such a dispute.

Competition

As noted above, the regulatory environment in which the Company operates is changing rapidly. The passage of the Telecom Act combined with other actions by the FCC and state regulatory authorities continues to promote competition in the provision of telecommunications services.

ILECs

In each market served by its networks, the Company faces, and expects to continue to face, significant competition from the ILECs, which currently dominate their local telecommunications markets.

The Company competes with the ILECs in its markets for local exchange services on the basis of product offerings, reliability, state-of-the-art technology, price, route diversity, ease of ordering and customer service. However, the ILECs have long-standing relationships with their customers and provide those customers with various transmission and switching services that the Company, in many cases, does not currently offer. The Company has sought, and will continue to seek, to achieve parity with the ILECs in order to become able to provide a full range of local telecommunications services. See "Regulatory Overview" for additional information concerning the regulatory environment in which the Company operates. Existing competition for private line and special access services is based primarily on quality, capacity and reliability of network facilities, customer service, response to customer needs, service features and price, and is not based on any proprietary technology. As a result of the comparatively recent installation of the Company's fiber optic networks, its dual path architectures and the state-of-the-art technology used in its networks, the Company may have cost and service quality advantages over some currently available ILEC networks.

Other Competitors

The Company also faces, and expects to continue to face, competition from other potential competitors in certain of the markets in which the Company offers its services. In addition to the ILECs and CAPs, potential competitors capable of offering switched local and long distance services include long distance carriers such as AT&T, MCI Communications Corporation ("MCI"), Sprint Corporation ("Sprint") and WorldCom, Inc. ("WorldCom"), cable television companies such as TeleCommunications, Inc. and Time Warner, Inc., electric utilities, microwave carriers, wireless telephone system operators and private networks built by large end users.

The Company believes that the Telecom Act, as well as a recent series of completed and proposed transactions between ILECs and long distance companies and cable companies, increases the likelihood that barriers to local exchange competition will be removed. The Telecom Act states that entry barriers must be lowered in the areas served by ILECs that are subsidiaries of RBOCs before such ILECs are permitted to provide in-region, interLATA services. When ILECs that are RBOC subsidiaries are permitted to provide such services, they will be in a position to offer single source service. ILECs that are not RBOC subsidiaries may offer single source service presently.

In some cases, cable television companies are upgrading their networks with fiber optics and installing facilities to provide fully interactive transmission of broadband voice, video and data communications. In addition, under the Telecom Act, electric utilities may install fiber optic telecommunications cable and may facilitate provision of telecommunications services by electric utilities over those networks if granted regulatory authority to do so. Cellular and PCS providers may also be a source of competitive local telephone service.

The Company also competes with equipment vendors and installers, and telecommunications management companies, with respect to certain portions of its business.

A continuing trend towards business combinations and alliances in the telecommunications industry may create significant new competitors to the Company. In addition, many of the Company's existing and potential competitors have financial, personnel and other resources, including name recognition, significantly greater than those of the Company.

The Company also competes with long distance carriers in the provision of long distance services. Although the long distance market is dominated by four major competitors, AT&T, MCI, Sprint and WorldCom, hundreds of other companies also compete in the long distance marketplace.

With respect to the Company's enhanced communications service offerings, each is subject to competition. For example, there are several competitors that offer IVR services, such as Call Interactive, which the Company believes focuses its sales efforts on large volume IVR service users. Another competitor, Telemedia, which is owned by Sprint, also offers significant call volume capacity. With respect to Magic Number, the Company's virtual communications center, there are numerous competitors with product offerings that include some or all of the services offered by Magic Number.

Purchasing and Distribution

With respect to the Company's fiber optic networks, which constitute the Company's most significant capital investments, the Company has entered into general purchase agreements with key equipment suppliers for fiber and fiber optic transmission equipment, with Nortel for telecommunications switches, and with other suppliers for various other components of each system. These agreements provide the basic framework under which purchase orders for these system components will be made. The specific purchases made for each network depend upon the configuration and other factors related to the network, such as the prospective customer base and location and the services to be offered over the network. Once these decisions are made, purchase orders for the appropriate fiber and selected equipment types are placed under the general purchase agreements. In connection with the Company's provision of long distance services, it purchases capacity at wholesale rates from long distance carriers.

Employees

As of December 31, 1997, the Company employed 1,327 people, including full-time and part-time employees. The Company considers its employee relations to be good. None of the employees of the Company is covered by a collective bargaining agreement.

Trademarks and Trade Names

The Company uses the name "NEXTLINK" as its primary business name. In July 1995, the Company filed for federal trademark protection of this name and received its notice of allowance from the U.S. Patent and Trademark Office (the "PTO") on July 1, 1997. In addition, the Company has received a notice of allowance from the PTO of its distinctive floating "X" and related marks as protected trademarks under federal law. The Company from time to time receives requests to consider licensing certain patents held by third parties that may have bearing on its IVR and virtual communications center services. The Company considers such requests on their merits, but has not to date entered into any such license agreements.

Glossary

Addressable business lines — In accordance with industry practice, the Company includes in its calculation of actual and targeted addressable business lines all business lines currently in active use through any service provider in each market area in which the Company has or plans to build a network.

CAP (competitive access provider) — A company that provides its customers with an alternative to the ILEC for local private line and special access telecommunications services.

Central offices — The switching centers or central switching facilities of the LECs.

CLEC (competitive local exchange carrier) — A company providing local telephone services in competition with the ILEC.

Co-carrier status — A regulatory scheme under which the ILEC is required to integrate new, competing providers of local exchange service, such as the Company, into the systems of traffic exchange, inter-carrier compensation, and other inter-carrier relationships that already exist among ILECs in most jurisdictions.

Collocation — The ability of a CLEC such as the Company to connect its network to the ILECs' central offices. Physical collocation occurs when a CLEC places its network connection equipment inside the ILEC's central offices. Virtual collocation is an alternative to physical collocation pursuant to which the ILEC permits a CLEC to connect its network to the ILEC's central offices on comparable terms, even though the CLEC's network connection equipment is not physically located inside the central offices.

Dark fiber — Unused fiber through which no light is transmitted. Dark fiber is provided with the customer expected to supply the required electronics and signals.

Dedicated — Telecommunications lines dedicated or reserved for use by particular customers and charged on a flat, usually monthly, basis.

DS-0, DS-1, DS-3 — The standard circuit capacity classifications. Each of these transmission services can be provided using the same type of fiber optic cable, but offer different bandwidth (that is, capacity), depending upon the individual needs of the end user. A DS-0 is a dedicated circuit that is considered to meet the requirements of usual business communications, with transmission capacity of up to 64 kilobits of bandwidth per second (that is, a voice grade equivalent circuit). This service offers a basic low capacity dedicated digital line for connecting telephones, fax machines, personal computers and other telecommunications equipment. A DS-1 is a high speed digital circuit typically linking high volume customer locations to long distance carriers or other customer locations. Typically utilized for voice transmissions as well as the interconnection of LANs, DS-1 service accommodates transmission speeds of up to 1.544 megabits per second, which is the equivalent of 24 voice grade equivalent circuits. DS-3 service provides a very high capacity digital circuit with transmission capacity of 45 megabits per second, which is equivalent to 28 DS-1 circuits or 672 voice grade equivalent circuits. This is a digital service used by long distance carriers for central office connections and by some large commercial users to link multiple sites.

FCC — The United States Federal Communications Commission.

FDDI (fiber distributed data interface) — Based on fiber optics, FDDI is a 100 megabit per second local area network technology used to connect computers, printers, and workstations at very high speeds. FDDI is also used as backbone technology to interconnect other LANs.

Fiber mile — The number of route miles installed (excluding pending installations) along a telecommunications path multiplied by the number of fibers along that path. See the definition of "route mile" below.

ILEC (incumbent local exchange carrier) — A company that was providing local exchange service prior to the entry of the CLECs.

Local Exchange — A geographic area determined by the appropriate state regulatory authority in which calls generally are transmitted without toll charges to the calling or called party.

Line — An electrical path between an ILEC central office and a subscriber.

Long distance carriers (interexchange carriers) — Long distance carriers provide services between local exchanges on an interstate or intrastate basis. A long distance carrier may offer services over its own or another carrier's facilities.

Number Portability — The ability of an end user to change local exchange carriers while retaining the same telephone number.

POPs (points of presence) — Locations where a long distance carrier has installed transmission equipment in a service area that serves as, or relays calls to, a network switching center of that long distance carrier.

PUC (public utility commission) — A state regulatory body, established in most states, which regulates utilities, including telephone companies, providing intrastate services.

Private line — A dedicated telecommunications connection between end user locations.

Reciprocal compensation — The compensation paid to and from a new competitive local exchange carrier and the ILEC for termination of a local call on each other's networks.

Route mile — The number of miles of the telecommunications path in which the Company-owned or leased fiber optic cables are installed.

Special access services — The lease of private, dedicated telecommunications lines or "circuits" along the network of an ILEC or a CAP, which lines or circuits run to or from the long distance carrier POPs. Examples of special access services are telecommunications lines running between POPs of a single long distance carrier, from one long distance carrier POP to the POP of another long distance carrier or from an end user to a long distance carrier POP.

Switch — A device that opens or closes circuits or selects the paths or circuits to be used for transmission of information. Switching is a process of interconnecting circuits to form a transmission path between users.

Switched services — Transmission of switched calls through the local switched network.

Item 2. *Description of Properties*

The Company owns or leases, in its operating territories, telephone property which includes: fiber optic backbone and distribution network facilities; point-to-point distribution capacity; central office switching equipment; connecting lines between customers' premises and the central offices; and customer premise equipment.

The fiber optic backbone and distribution network and connecting lines include aerial and underground cable, conduit, and poles and wires. These facilities are located on public streets and highways or on privately owned land. The Company has permission to use these lands pursuant to consent or lease, permit, easement, or other agreements. The central office switching equipment includes electronic switches and peripheral equipment.

The Company and its subsidiaries lease facilities for their administrative and sales offices, network nodes and warehouse space. The various leases expire in years ranging from 1998 to 2028. Most have renewal options. Additional office space and equipment rooms will be leased as the Company's operations and networks are expanded and as new networks are constructed.

Item 3. *Legal Proceedings*

The Company is not currently a party to any legal proceedings, other than regulatory and other proceedings that are in the normal course of its business.

Item 4. *Submission of Matters to a Vote of Security Holders*

No matters were submitted to a vote of security holders during the quarter ended December 31, 1997.

PART II

Item 5. *Market for Registrants' Common Stock and Related Stockholder Matters*

Market Information

The Company's Class A Common Stock began trading on the Nasdaq National Market on September 26, 1997, under the symbol "NXLK". Prior to that date, the Company's Class A Common Stock was not publicly traded. The following table shows, for the periods indicated, the high and low bid prices for the

Company's Class A Common Stock as reported by the Nasdaq National Market tier of The Nasdaq Stock Market.

	High	Low
1997:		
Third Quarter (since September 26, 1997)	$25.50	$23.13
Fourth Quarter	$27.75	$19.50

There is no public trading market for the Company's Class B Common Stock or NEXTLINK Capital's common equity.

As of March 6, 1998, the approximate number of shareholders of record of the Company's Class A and Class B Common Stock was 218 and 15, respectively. The Company is the sole holder of record of NEXTLINK Capital's Common Stock.

Use of Proceeds

The Company filed a registration statement on Form S-1 (File No. 333-32001) which became effective on September 26, 1997, whereby 15,200,000 shares of Class A Common Stock , $0.02 par value per share, were sold in an initial public offering at a price of $17 per share. Of the 15,200,000 shares of Class A Common Stock sold, 12,000,000 shares were sold by the Company and 3,200,000 shares were sold by a selling shareholder. The Company did not receive any of the proceeds from the sale of shares by the selling shareholder. In addition, the underwriters of the IPO, led by Salomon Smith Barney, exercised an option to purchase 2,280,000 additional shares of Class A Common Stock at the same price per share. Net proceeds to the Company from the IPO totaled approximately $226.8 million, after deducting underwriting discounts, advisory fees and expenses aggregating approximately $16.0 million. The Company intends to use substantially all of the net proceeds from the IPO for expenditures relating to the expansion of existing networks and services, the development and acquisition of new networks and services and the funding of operating losses and working capital. None of the net proceeds from the IPO had been used by the Company as of December 31, 1997.

The Company filed a registration statement on Form S-1 (File No. 333-32003) which became effective on September 26, 1997, whereby the Company sold $400 million aggregate principal amount of 9⅝% Senior Notes due 2007 ("9⅝% Senior Notes"). The offering was led by Salomon Smith Barney. Net proceeds from the sale of the 9⅝% Senior Notes totaled approximately $388.5 million, after deducting issuance costs aggregating approximately $11.5 million, relating to underwriting discounts, advisory fees and expenses. The use of proceeds from the debt offering are substantially the same as the Company's IPO. None of the net proceeds from the sale of 9⅝% Senior Notes had been used by the Company as of December 31, 1997.

Dividends

Neither the Company nor NEXTLINK Capital have declared a cash dividend on any of their respective equity securities. Covenants in the indentures pursuant to which the Company's and NEXTLINK Capital's Senior Notes have been issued restrict the ability of the Company to pay cash dividends on its capital stock.

Sales of Unregistered Securities

None.

Item 6. *Management's Discussion and Analysis of Financial Condition and Results of Operations*

Overview

Since its inception in 1994, the Company has executed a strategy of developing fiber optic networks and acquiring related telecommunications businesses. Over this period, the Company has pursued this strategy by constructing, acquiring, leasing fibers or capacity on, and entering into agreements to acquire telecommunications networks.

The Company's primary focus is providing switched local and long distance and enhanced communications services to small and medium-sized commercial end user customers. The Company plans to acquire, build or develop networks in new areas, expand its current networks, and also explore the acquisition or licensing of additional enhanced communications services and other telecommunications service providers. These efforts should allow the Company to increase its presence in the marketplace, and facilitate providing a single source solution for the telecommunications needs of its customers.

The table provides selected key operational data:

	As of December 31, 1997	1996
Operating data (1):		
Route miles(2)	1,897	1,080
Fiber miles(3)	133,224	66,046
On-net buildings connected(4)	513	403
Off-net buildings connected(5)	3,504	—
Switches installed	13	9
Access lines in service(6)	50,131	8,511
Employees	1,327	568

(1) The operating data include the statistics of the Las Vegas network, which the Company manages and in which the Company has a 40% membership interest.

(2) Route miles refers to the number of miles of the telecommunications path in which the Company-owned or leased fiber optic cables are installed.

(3) Fiber miles refers to the number of route miles installed along a telecommunications path, multiplied by the Company's estimate of the number of fibers along that path.

(4) Represents buildings physically connected to the Company's networks, excluding those connected by unbundled incumbent local exchange (ILEC) facilities.

(5) Represents buildings connected to the Company's networks through leased or unbundled ILEC facilities.

(6) Represents the number of access lines in service, including those lines which are provided through resale of Centrex services, for which the Company is billing services.

The Company builds its networks to encompass the significant business concentrations in each area it serves, focusing on direct connections to end user locations and ILEC central offices. The Company employs a uniform technology platform for each of its local exchange networks that is based on the Nortel DMS 500 digital local and long distance combination switching platform and associated distribution technology. As of January 31, 1998, the Company had 12 operational Nortel DMS 500 switches, including one switch in its NEXTLAB facility, and currently plans to install three additional switches by the end of the second quarter of 1998. NEXTLAB is a fully functional model of one of the Company's networks, which serves as a testing facility for switch software and the Company's products and services and will serve as the Company's network operations control center.

The Company also provides enhanced communications services including interactive voice response ("IVR") services, which provide an interface between the Company's clients and their customers for a variety of applications. Historically, the Company has derived a substantial proportion of its revenues from these IVR services. As local and long distance revenues are expected to grow more rapidly than revenues for the Company's enhanced communications services, the Company anticipates that, over the next five years, local and long distance revenues will account for a significantly higher percentage of total revenues.

The development of the Company's businesses and the construction, acquisition and expansion of its networks require significant expenditures, a substantial portion of which are incurred before the realization of revenues. These expenditures, together with the associated early operating expenses, result in negative cash flow until an adequate customer base is established. However, as the customer base grows, the Company expects that incremental revenues can be generated with decreasing incremental operating expenses, which may provide positive contributions to cash flow. The Company has made the strategic decision to build high capacity networks with broad market coverage, which initially increases its level of capital expenditures and operating losses. The Company believes that over the long term this will enhance the Company's financial performance by increasing the traffic flow over the Company's networks. The Company has recently entered into leased dark fiber and fiber capacity arrangements, which allow the Company, by installing one or more switches and related electronics, to enter a market prior to completing construction of its own fiber optic network.

Prior to January 31, 1997, the Company was a limited liability company that was classified and taxed as a partnership for federal and state income tax purposes. As of January 31, 1997, the Company was subject to federal and state income tax.

Results of Operations

Year Ended December 31, 1997 Compared with Year Ended December 31, 1996

Revenue increased 124% to $57.6 million in 1997 from $25.7 million in the same period in 1996. The increase was primarily due to 45% growth in the Company's local and long distance services (both switched and resale), dedicated services and enhanced communications services, as well as due to recording a full year's revenue from ITC, a switch-based long distance reseller acquired in December 1996. To a lesser extent, the acquisitions of Start Technologies Corporation ("Start") and Chadwick Telecommunications Corporation ("Chadwick") in the fourth quarter of 1997 also contributed to the increase in revenue. Revenues reported in 1997 included $38.9 million derived from local and long distance, competitive access, dedicated line services and shared tenant services and $18.7 million derived from enhanced communications services, primarily IVR. The Company's IVR subsidiary contributed 27% and 52% of the Company's revenues during 1997 and 1996, respectively. The revenues generated by this subsidiary have tended to fluctuate on a quarter to quarter basis as the revenues are generally event driven and seasonal in nature.

The Company began offering switched local and long distance services in seven of its markets in July 1996, and in 18 additional markets during 1997. In addition, the Company has offered dedicated line services since January 1995 and has resold Centrex access lines since April 1995. The Company increased its quarterly customer access line installation rate from 1,604 in the fourth quarter of 1996 to 19,187 during the fourth quarter of 1997. As of December 31, 1997, the Company had 50,131 access lines in service, compared to 8,511 as of December 31, 1996. Revenues from the provision of such services are expected to continue to increase as a component of total revenues over future periods. Access lines in service includes those lines which are provided through resale of Centrex services, the number of which is decreasing over time as the Company converts those customers to its own network.

Operating expenses consist of costs directly related to providing facilities-based network and enhanced communications services and also include salaries and benefits and related costs of operations and engineering personnel. Operating expenses increased 115% in 1997 to $54.0 million, an increase of $28.9 million over the same period in 1996. These increases were attributed to factors that include an increase in network costs related to the provision of increased volumes of local, long distance and enhanced communications services and the Company's increase in employees as well as other related costs primarily to expand the Company's switched local and long distance service businesses in its existing and planned markets. Additionally, the effects of the ITC acquisition in December 1996 and the two acquisitions in the fourth quarter of 1997 further resulted in an increase in 1997 operating expenses over those of the prior year.

Selling, general and administrative expenses ("SG&A") include salaries and related personnel costs, facilities expenses, sales and marketing, consulting and legal fees and equity in loss of affiliates. SG&A increased 142% for the year ended December 31, 1997 as compared to the corresponding period in 1996. The increase was primarily due to the Company's increase in employees and other costs associated with the expansion of the Company's switched local and long distance service businesses in its existing and planned markets, as well as the ITC acquisition.

Deferred compensation expense was recorded in connection with the Company's Equity Option Plan until April 1997, and in connection with the Company's Stock Option Plan (the "Plan"), which replaced the Equity Option Plan, subsequent to April 1997. The stock options granted under the Equity Option Plan were considered compensatory and were accounted for on a basis similar to that for stock appreciation rights. All options outstanding under the Equity Option Plan were regranted under the new Plan with terms and conditions substantially the same as under the Equity Option Plan. As such, the Company continues to record deferred compensation expense for those compensatory stock options issued, as well as for compensatory stock options issued subsequent to the Plan conversion date. Compensation expense is recognized over the vesting periods based on the excess of the fair value of the stock options at the date of grant over the exercise price.

Depreciation expense increased primarily due to placement in service of additional telecommunications network assets, including switches, fiber optic cable, network electronics and related equipment. Amortization of intangible assets increased primarily as a result of the ITC acquisition in December 1996, as well as the acquisitions of Linkatel, Start and Chadwick in 1997.

Interest expense increased 76% in 1997 over the prior year due to an increase in the Company's average outstanding indebtedness over the respective periods, primarily relating to the 12½% and 9⅝% Senior Notes issued in April 1996 and October 1997, respectively. See "— Liquidity and Capital Resources." Pursuant to Statement of Financial Accounting Standards No. 34, the Company capitalizes a portion of its interest costs as part of the construction cost of its communications networks. Capitalized interest during 1997 totaled $1.8 million. Interest income results from investment of excess cash and certain securities that have been pledged as collateral for interest payments on the 12½% Senior Notes. The increase in interest income in 1997 over 1996 corresponded to the increase in the Company's average outstanding cash balances.

Liquidity and Capital Resources

The competitive local telecommunications service business is a capital intensive business. The Company's existing operations have required and will continue to require substantial capital investment for the acquisition and installation of fiber, electronics and related equipment in order to provide switched services in the Company's networks and the funding of operating losses during the start-up phase of each market. In addition, the Company's strategic plan calls for expansion into additional market areas. Such expansion will require significant additional capital for: potential acquisitions of businesses or assets; design, development and construction of new networks; and the funding of operating losses during the start-up phase of each market. During 1997, the Company used $94.5 million in cash for operating activities, compared to $40.6 million in 1996. The increase was primarily due to a substantial increase in the Company's activities associated with the development and initiation of switched local and long distance services. In addition, during 1997, the Company invested an additional $210.5 million in cash in property and equipment, acquisitions of telecommunications businesses and equity investments in telecommunications businesses. During 1996, the Company invested $78.0 million in cash in property and equipment, acquisitions of telecommunications assets and businesses and equity investments in telecommunications businesses.

In February 1998, the Company signed a definitive agreement with Metromedia Fiber Network for exclusive rights to multiple fibers and innerducts for 20 years, with two 10 year renewals. The route covered by the agreement extends over 650 route miles from Manhattan to White Plains (NY), to Stamford (CT), to Newark (NJ) and south from Manhattan through Philadelphia, Wilmington (DE), Baltimore, and to Washington (DC). The route will offer frequent splice points within metropolitan areas and splice points at least every 10,000 feet on routes between metropolitan areas, as well as provide access to ILEC central and tandem switching offices. The Company will pay $92.0 million in cash for the transaction, of which $80.3 million will be placed into escrow, to be released as segments of the route are constructed and delivered to the Company.

In January 1998, the Company and Nextel formed NEXTBAND, a joint venture which is owned 50% by the Company and 50% by Nextel. On January 20, 1998, NEXTBAND filed an application with the FCC for which it paid a $50.0 million refundable deposit to participate in the FCC's LMDS auction which began on February 18, 1998. Of the deposit amount, $25.0 million was contributed by the Company. LMDS is a fixed broadband point-to-multipoint service which the FCC and industry analysts anticipate will be used for the deployment of wireless local loop, high-speed data transfer and video broadcasting services. Two licenses will be awarded in each of 493 BTAs when the auction is concluded. Although the number of licenses that may be awarded to NEXTBAND is limited by the amount of the deposit, NEXTBAND has applied for and is eligible to bid on any of the markets being auctioned for the block A license (1,150 MHz of spectrum) and the block B license (150 MHz of spectrum).

The Company is exploring LMDS for two reasons. Depending upon the bidding and deployment costs, LMDS may offer an economically efficient means to supplement the Company's fiber network build-out in some localities. In addition, a wireless local loop alternative may create competitive pressure on high unbundled loop costs in certain areas. There can be no assurance that NEXTBAND's participation in the auction will result in the purchase of any LMDS licenses or that LMDS spectrum for wireless connectivity will provide a cost-effective and efficiently engineered means to connect to end user locations. If NEXTLINK's bids are successful, the purchase price of the licenses and the costs of building out any such wireless systems could be substantial.

In November 1997, the Company acquired all outstanding shares of Start, a shared tenant services provider serving commercial buildings in Dallas, Austin and Corpus Christi, Texas and Phoenix, Arizona. Services offered by Start include local and long distance services, Internet access and customer premise equipment management. Start currently provides services under long term contracts to 600 corporate customers, or approximately 13,000 end users. The Company paid consideration for the transaction consisting of \$20.0 million in cash, 441,336 shares of Class A common stock and the assumption of approximately \$5.3 million of liabilities, the majority of which were repaid.

In October 1997, the Company acquired all of the outstanding shares of Chadwick, a switch-based long distance reseller in central Pennsylvania, through a merger transaction between Chadwick and a wholly owned subsidiary of NEXTLINK. Chadwick serves approximately 11,500 customers throughout the central and eastern Pennsylvania regions. The Company issued consideration for the transaction consisting of a promissory note payable in the aggregate principal amount of \$5.0 million (which was repaid in full in January 1998), 257,151 shares of Class A Common Stock and the repayment of long term debt and other liabilities totaling \$6.6 million. The merger agreement also provides for additional payments of up to a maximum of 192,863 shares of Class A Common Stock over a two year period, with these payments being contingent upon the acquired operation achieving specified performance goals.

In September 1997, the Company entered into a definitive agreement to acquire certain telecommunications assets of Unicom Thermal Technologies, Inc. ("UTT"), including two existing route miles of network plus 13 miles of conduit in downtown Chicago. The Company also has the right to participate in the ongoing expansion of UTT's network in Chicago. The existing network currently provides connectivity to 28 buildings. The Company agreed to pay \$2.5 million in cash, plus up to an additional \$560,000 for the acquisition of certain additional telecommunications facilities. The Company will also be required to pay certain additional consideration to UTT for a portion of the network expansion costs, up to \$3.4 million in cash plus the issuance of up to 60,022 shares of Class A Common Stock.

In June 1997, the Company entered into an eight year exclusive agreement, with an option to renew for five additional years, with a company that has excess fiber capacity in each of Atlanta, Chicago, New York City, Newark (NJ) and Philadelphia which it agreed to make available to the Company in each of those markets at a substantial discount to the wholesale rates charged by other vendors of capacity. In addition to the capacity arrangement described above, the Company also has entered into a 20-year lease of capacity over an existing 47-mile fiber network in New York City, which extends from the Wall Street area north to midtown Manhattan. In June 1997, the Company paid \$11 million in full satisfaction of its obligations under this lease, \$6 million of which was placed in escrow pending completion of certain building connections by the lessor. As of December 31, 1997, \$4.1 million remained in escrow. These arrangements will allow the Company to accelerate its entry into each of these markets by enabling the Company to avoid a significant portion of the infrastructure development and construction time that would otherwise be required to launch switched local and long distance services in these markets. Although these agreements have reduced the initial capital expenditures necessary to enter these markets, the Company has not, as a result, reduced its overall planned capital expenditures through 1999.

In June 1997, the Company also executed a definitive agreement to acquire an existing fiber optic network in downtown Philadelphia in order to extend its existing network in Pennsylvania. The acquisition is subject to regulatory and other consents and is anticipated to be consummated by the end of the second quarter in 1998. During the interim period prior to closing, the Company is operating under a 36 fiber capacity agreement with the seller.

On February 4, 1997, the Company completed the acquisition of substantially all of the assets of Linkatel, a Los Angeles-based competitive access telecommunications provider. At the time of acquisition, Linkatel operated an 80 mile fiber optic telecommunications network covering several markets in the Orange and Los Angeles county areas. The total purchase price of $42.5 million consisted of a cash payment of $36.1 million (including the release of $6.0 million which was deposited into escrow during 1996) plus the repayment of debt of $5.6 million and the assumption of net liabilities totaling $0.8 million.

In January 1997, the Company obtained rights-of-way to expand its existing Salt Lake City network into Provo and Orem, Utah. The Company has completed the expansion of this network to Provo and Orem and began providing switched local and long distance services in Provo and Orem in September 1997.

Prior to April 1996, the Company funded its expenditures with approximately $55.0 million of cash equity investments from two entities that are controlled by Craig O. McCaw. On April 25, 1996, the Company raised gross proceeds of $350.0 million through the issuance of 12½% Senior Notes due April 15, 2006 ("12½% Senior Notes"). The Company used $117.7 million of the gross proceeds to purchase and hold in escrow U.S. government securities, representing funds sufficient to provide for payment in full of interest on the 12½% Senior Notes through April 15, 1999, and used an additional $32.2 million to repay certain advances and accrued interest from Eagle River, a company majority-owned and controlled by Mr. McCaw. In addition, the Company incurred costs of $9.8 million in connection with the financing. Interest payments on the 12½% Senior Notes are due semi-annually.

On January 31, 1997, the Company completed the sale of $285 million aggregate liquidation preference of 14% senior exchangeable redeemable preferred shares ("Preferred Shares") which, after deducting issuance costs, resulted in net proceeds to the Company of approximately $274 million. The Preferred Shares accrue dividends at the rate of 14% per annum. On or before February 1, 2002, dividends may, at the option of the Company, be paid in cash or by issuing additional Preferred Shares with an aggregate liquidation preference equal to the amount of such dividends. After February 1, 2002, dividends must be paid in cash. As of December 31, 1997, the Company had issued an additional 622,031 shares of Preferred Shares in satisfaction of the first three quarterly dividends.

Since inception and through December 1996, the Company has also issued Class A Units valued at $15.5 million primarily for the acquisition of certain telecommunications assets and businesses, which Units were converted to shares of Class B Common Stock of the Company on January 31, 1997.

On October 1, 1997, the Company completed an initial public offering ("IPO") of 12,000,000 shares of Class A Common Stock at a price of $17 per share. In addition, the underwriters of the IPO exercised an option to purchase 2,280,000 additional shares of Class A Common Stock at the same price per share. Gross proceeds from the IPO totaled $242.8 million, and proceeds net of underwriting discounts, advisory fees and estimated expenses aggregated approximately $226.8 million. Concurrently with the IPO, the Company sold $400 million in aggregate principal amount of 9¾% Senior Notes due 2007, which, after deducting estimated issue costs, resulted in net proceeds to the Company of approximately $388.5 million. Interest payments on the 9¾% Senior Notes are due semi-annually.

On March 3, 1998, the Company completed the sale of $335 million in aggregate principal amount of 9% Senior Notes due 2008 ("9% Senior Notes"). Proceeds from the sale, net of discounts, underwriting commissions, advisory fees and expenses, totaled approximately $326.5 million. Interest payments on the 9% Senior Notes are due semi-annually, beginning September 1998.

The Company will use the remaining proceeds from the sale of Class A Common Stock, 9⅝% Senior Notes and 9% Senior Notes and existing unrestricted cash balances for expenditures relating to the construction, acquisition and operation of telecommunications networks and service providers and the offering of telecommunications services in those areas where the Company currently operates or intends to operate. Expenditures for the construction and operation of networks include (i) the purchase and installation of switches and related electronics in existing networks and in networks to be constructed or acquired in new or adjacent markets; (ii) the purchase and installation of fiber optic cable and electronics to expand existing networks and develop new networks, including the connection of new buildings; (iii) spectrum that may be purchased during the LMDS auction that is currently ongoing; (iv) the development of its comprehensive information technology platform and (v) the funding of operating losses and working capital. The Company may also acquire or invest in businesses that consist of existing networks or companies engaged in businesses similar to those engaged in by the Company and its subsidiaries or other complementary businesses.

As of December 31, 1997, the Company had unrestricted cash and investments of $742.4 million and $1,068.9 million on a pro forma basis after giving effect to the sale of the 9% Senior Notes. The Company's current plan contemplates an aggressive expansion into a number of new markets throughout the United States. The Company may pursue various alternatives for achieving its growth strategy, including: additional network construction; additional leases of network capacity from third party providers; acquisitions of existing networks; and spectrum that may be purchased during the LMDS auction that is currently ongoing and associated facilities construction and deployment if any spectrum is purchased. The Company also anticipates that a substantial amount of additional capital expenditures will be made in 1999 and beyond. The funding of these capital expenditures is expected to be provided by existing cash balances, future vendor and/or credit facilities, future public or private sales of debt securities, future sales of public or private capital stock and joint ventures. There can be no assurance, however, that the Company will be successful in raising sufficient additional capital on terms that it will consider acceptable or that the Company's operations will produce positive consolidated cash flow in sufficient amounts to meet its interest and dividend obligations on outstanding securities. Failure to raise and generate sufficient funds may require the Company to delay or abandon some of its planned future expansion or expenditures, which could have a material adverse effect on the Company's growth and its ability to compete in the telecommunications services industry.

In addition, the Company's operating flexibility with respect to certain business matters is, and will continue to be, limited by covenants associated with the 12½% Senior Notes, the 9⅝% Senior Notes and the 9% Senior Notes. Among other things, these covenants limit the ability of the Company and its subsidiaries to incur additional indebtedness, create liens upon assets, apply the proceeds from the disposal of assets, make dividend payments and other distributions on capital stock and redeem capital stock. In addition, the terms of the Preferred Shares contain certain covenants that may limit the Company's operating flexibility with respect to the incurrence of indebtedness and issuance of additional preferred shares. There can be no assurance that such covenants will not adversely affect the Company's ability to finance its future operations or capital needs or to engage in other business activities that may be in the interest of the Company. The Company was in compliance with all covenants associated with the 12½% Senior Notes, the 9⅝% Senior Notes and the Preferred Shares as of December 31, 1997.

Impact of Year 2000

Certain of the Company's older computer systems and applications were written to define a given year with abbreviated dates using the last two digits in a year rather than the entire four digits. As a result, those systems and applications have time-sensitive software that recognize an abbreviated year "00" as the year 1900 rather than the year 2000. This could cause a system failure or miscalculations resulting in disruptions of operations including, among other things, a temporary inability to process transactions, send invoices or engage in other normal business activities.

The Company has received positive confirmation from its vendor that the Company's Nortel DMS 500 switches and related telecommunications equipment are Year 2000 compliant. The Company is currently assessing the extent of replacements or modifications necessary to certain of its older computer systems and applications so that such systems and applications will properly utilize dates beyond December 31, 1999. The

Company believes that the impact of upgrading or modifying existing software and converting to new software (the "Year 2000 Project") will not be material to the Company operations or financial position. Costs incurred in connection with the Year 2000 project will be expensed as incurred unless new software is purchased, in which case such costs will be capitalized. The Company has not incurred significant Year 2000 project costs to date. The Company plans to complete the Year 2000 project no later than December 31, 1998.

Outlook: Issues and Uncertainties

The Company does not provide forecasts of future financial performance. This Report, however, does contain statements that are not historical facts and are forward-looking. Actual events or results may differ materially from events or results indicated, whether expressed or implied. Although the Company's management is optimistic about the Company's long-term prospects, the following issues and uncertainties, among others, should be considered in evaluating its outlook.

Negative Cash Flow and Operating Losses; Limited History of Operations

The development of the Company's businesses and the installation and expansion of its networks require significant expenditures, a substantial portion of which must be made before any revenues may be realized. Certain of the expenditures are expensed as incurred, while certain other expenditures are capitalized. These expenditures, together with the associated early operating expenses, result in negative cash flow and operating losses until an adequate revenue base is established. There can be no assurance that an adequate revenue base will be established for any of the Company's networks. The Company's operations have resulted in net losses of $12.7 million, $71.1 million and $129.0 million for the years ended December 31, 1995, 1996 and 1997, respectively. The Company will continue to incur significant expenditures in the future in connection with the acquisition, development and expansion of its networks, services and customer base. There can be no assurance that the Company will achieve or sustain profitability or generate positive cash flow in the future.

The Company was formed in September 1994. A significant, but declining, portion of the Company's revenue for the years ended December 31, 1995, 1996 and 1997, was derived from the operations of the Company's IVR enhanced service offering, which operations were acquired by the Company in September 1995. Prospective investors, therefore, have limited historical financial information upon which to base an evaluation of the Company's performance in the business which will be its principal focus in the future. The Company has only recently commenced operations as a single source service provider of telecommunications services. Given the Company's limited operating history, there can be no assurance that it will be able to complete successfully in the telecommunications business and to generate positive cash flow in the future.

Significant Future Capital Requirements; Substantial Indebtedness

Expansion of the Company's existing networks and services and the development and acquisition of new networks and services will require significant capital expenditures. The Company will also continue to evaluate additional revenue opportunities in each of its markets and, as and when attractive additional opportunities develop, the Company plans to make capital investments in its networks that might be required to pursue such opportunities. The Company expects to meet its additional capital needs with the proceeds from credit facilities and other borrowings, the proceeds from public or private sales of debt securities, the sale or issuance of equity securities and through joint ventures. There can be no assurance, however, that the Company will be successful in raising sufficient additional capital on terms that it will consider acceptable or that the Company's operations will produce positive cash flow in sufficient amounts to service its debt and to pay cash dividends on the 14% Preferred Shares. Failure to raise and generate sufficient funds may require the Company to delay or abandon some of its planned future expansion or expenditures, which could have a material adverse effect on the Company's growth and its ability to compete in the telecommunications services industry. See "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources."

The Company expects to incur substantial additional indebtedness (including secured indebtedness) during the next few years to finance the acquisition, construction and expansion of networks, the potential acquisition of telecommunications companies, the possible acquisition of LMDS spectrum and the construction and deployment of associated facilities, if such spectrum is purchased, the purchase of additional switches, the offering of switched local and long distance services, the introduction of other new service offerings and the development and implementation of a comprehensive information technology platform. The Indenture does not limit the amount the Company may invest in Restricted Subsidiaries or certain joint ventures engaged in one or more Telecommunications Businesses (including the joint venture through which the Company is participating in the LMDS auction) or the amount of Debt the Company may incur to fund investments in Restricted Subsidiaries or such joint ventures. As of December 31, 1997, after giving pro forma effect to the Offering, the amount of total consolidated liabilities of the Company would have been approximately $1,164.7 million.

The future funding requirements discussed above are based on the Company's current estimates. There can be no assurance that actual expenditures and funding requirements will not be significantly higher or lower.

Risk Associated with Implementation of Growth Strategy

The expansion and development of the Company's operations (including the construction and acquisition of additional networks) will depend on, among other things, the Company's ability to assess markets, identify, finance and complete suitable acquisitions, design fiber optic network backbone routes, install fiber optic cable and facilities, including switches, and obtain rights-of-way, building access rights and any required government authorizations, franchises and permits, all in a timely manner, at reasonable costs and on satisfactory terms and conditions. In addition, the Company has experienced rapid growth since its inception, and the Company believes that sustained growth places a strain on operational, human and financial resources. In order to manage its growth, NEXTLINK must continue to improve its operating and administrative systems including the continued development of effective systems relating to ordering, provisioning and billing for telecommunications services. NEXTLINK must also continue to attract and retain qualified managerial, professional and technical personnel. As a result, there can be no assurance that the Company will be able to implement and manage successfully its growth strategy. The Company's growth strategy also involves the following risks:

Qualified Personnel. NEXTLINK believes that a critical component for its success will be the attraction and retention of qualified managerial, professional and technical personnel. During 1997 the Company has experienced significant competition in the attraction and retention of personnel that possess the skill sets that the Company is seeking. Although the Company has been successful in attracting and retaining qualified personnel, there can be no assurance that NEXTLINK will not experience a shortage of qualified personnel in the future.

Switch and Equipment Installation. An essential element of the Company's current strategy is the provision of switched local service. There can be no assurance that the installation of the required switches, fiber optic cable and associated electronics necessary to implement the Company's business plan will continue to be completed on time or that, during the testing of these switches and related equipment, the Company will not experience technological problems that cannot be resolved. The failure of the Company to install and operate successfully additional switches and other network equipment could have a material adverse effect upon the Company's ability to enter additional markets as a single source provider of telecommunications services.

Interconnection Agreements. The Company has agreements or is currently negotiating agreements for the interconnection of its networks with the networks of the ILEC covering each market in which NEXTLINK either has or is constructing a network. NEXTLINK may be required to negotiate new, or renegotiate existing interconnection agreements as it enters new markets in the future. There can be no assurance that the Company will successfully negotiate such other agreements for interconnection with the ILEC or renewals of existing interconnection agreements. The failure to negotiate required interconnection agreements could have a material adverse effect upon the Company's ability to enter rapidly the telecommunications market as a single source provider of telecommunications services.

Ordering, Provisioning and Billing. The Company has developed processes and procedures and is working with external vendors, including the ILECs, in the implementation of customer orders for services, the provisioning, installation and delivery of such services and monthly billing for those services. In connection with its development of a comprehensive information technology platform, the Company is developing and implementing automated internal systems for processing customer orders and provisioning. Billing is provided by unaffiliated third-party vendors. The failure to develop effective internal processes and systems for these service elements or the failure of the Company's current vendors or the ILECs to deliver effectively ordering, provisioning (including establishing sufficient capacity and facilities on the ILEC's networks to service the Company) and billing services could have a material adverse effect upon the Company's ability to achieve its growth strategy.

Products and Services. The Company expects to continue to enhance its systems in order to offer its customers switched local services and other enhanced products and services in all of its networks as quickly as practicable and as permitted by applicable regulations. The Company believes its ability to offer, market and sell these additional products and services will be important to the Company's ability to meet its long-term strategic growth objectives, but is dependent on the Company's ability to obtain the needed capital, additional favorable regulatory developments and the acceptance of such products and services by the Company's customers. No assurance can be given that the Company will be able to obtain such capital or that such developments or acceptance will occur.

Acquisitions. The Company intends to use the net proceeds of the Offering to expand its networks and service offerings through internal developments and acquisitions, which could be material. Such acquisitions, if made, could divert the resources and management time of the Company and would require integration with the Company's existing networks and services. There can be no assurance that any such acquisitions will occur or that any such acquisitions, if made, would be on terms favorable to the Company or would be successfully integrated into the Company's operations.

Need To Obtain And Maintain Franchises, Permits And Rights-Of-Way

In order to acquire and develop its networks the Company must obtain local franchises and other permits, as well as rights to utilize underground conduit and aerial pole space and other rights-of-way and fiber capacity from entities such as ILECs and other utilities, railroads, long distance companies, state highway authorities, local governments and transit authorities. There can be no assurance that the Company will be able to maintain its existing franchises, permits and rights or to obtain and maintain the other franchises, permits and rights needed to implement its business plan on acceptable terms. Although the Company does not believe that any of the existing arrangements will be canceled or will not be renewed as needed in the near future, cancellation or non-renewal of certain of such arrangements could materially adversely affect the Company's business in the affected metropolitan area. In addition, the failure to enter into and maintain any such required arrangements for a particular network, including a network which is already under development, may affect the Company's ability to acquire or develop that network. See "Business — Company Network Architecture."

Competition

In each of the markets served by the Company's networks, the Company competes principally with the ILEC serving that area. ILECs are established providers of local telephone services to all or virtually all telephone subscribers within their respective service areas. ILECs also have long-standing relationships with regulatory authorities at the federal and state levels. While recent FCC administrative decisions and initiatives provide increased business opportunities to telecommunications providers such as the Company, they also provide the ILECs with increased pricing flexibility for their private line and special access and switched access services. In addition, with respect to competitive access services (as opposed to switched local exchange services), the FCC recently proposed a rule that would provide for increased ILEC pricing flexibility and deregulation for such access services either automatically or after certain competitive levels are reached. If the ILECs are allowed by regulators to offer discounts to large customers through contract tariffs, engage in aggressive volume and term discount pricing practices for their customers, and/or seek to charge competitors excessive fees for interconnection to their networks, the income of competitors to the ILECs, including the

Company, could be materially adversely affected. If future regulatory decisions afford the ILECs increased access services, pricing flexibility or other regulatory relief, such decisions could also have a material adverse effect on competitors to the ILEC, including the Company.

The Company also faces, and expects to continue to face, competition from other current and potential market entrants, including long distance carriers seeking to enter, reenter or expand entry into the local exchange market place such as AT&T Corp. ("AT&T"), MCI Communications Corporation ("MCI"), Sprint Corporation ("Sprint") and WorldCom, Inc. ("WorldCom"), and from other CLECs, competitive access providers ("CAPs"), cable television companies, electric utilities, microwave carriers, wireless telephone system operators and private networks built by large end-users. In addition, a continuing trend toward combinations and strategic alliances in the telecommunications industry could give rise to significant new competitors. The Telecom Act includes provisions which impose certain regulatory requirements on all local exchange carriers, including competitors such as the Company, while granting the FCC expanded authority to reduce the level of regulation applicable to any or all telecommunications carriers, including ILECs. The manner in which these provisions of the Telecom Act are implemented and enforced could have a material adverse effect on the Company's ability to successfully compete against ILECs and other telecommunications service providers. The Company also competes with equipment vendors and installers, and telecommunications management companies with respect to certain portions of its business. Many of the Company's current and potential competitors have financial, personnel and other resources, including brand name recognition, substantially greater than those of the Company, as well as other competitive advantages over the Company.

The Company also competes with long distance carriers in the provision of long distance services. Although the long distance market is dominated by four major competitors, AT&T, MCI, Sprint and WorldCom, hundreds of other companies also compete in the long distance marketplace.

Regulation

The Company is subject to varying degrees of federal, state and local regulation. In each state in which the Company desires to offer its services, the Company is required to obtain authorization from the appropriate state commission. Although the Company has received such authorization for each of its operational markets, there can be no assurance that the Company will receive such authorization for markets to be launched in the future. The Company is not currently subject to price cap or rate of return regulation, nor is it currently required to obtain FCC authorization for the installation, acquisition or operation of its network facilities. Further, the FCC has determined that non-dominant carriers, such as the Company and its subsidiaries, are not required to file interstate tariffs for interstate access and domestic long distance service on an ongoing basis. On February 13, 1997, the United States Court of Appeals for the District of Columbia granted motions for a stay on the FCC detariffing order pending judicial review of that order. The result of this stay is that carriers must continue to file tariffs for interstate long distance services. The FCC requires the Company and its subsidiaries to file interstate tariffs on an ongoing basis for interstate and international interexchange traffic. The Company's subsidiaries that provide or will provide intrastate services are also generally subject to certification and tariff or price list filing requirements by state regulators. Although passage of the Telecom Act should result in increased opportunities for companies that are competing with the ILECs, no assurance can be given that changes in current or future regulations adopted by the FCC or state regulators or other legislative or judicial initiatives relating to the telecommunications industry would not have a material adverse effect on the Company. In addition, although the Telecom Act provides incentives to the ILECs that are subsidiaries of Regional Bell Operating Companies ("RBOCs") to enter the long distance service market, there can be no assurance that these ILECs will negotiate quickly with competitors such as the Company for the required interconnection of the competitor's networks with those of the ILEC. On July 2, 1997, SBC Communications Inc. ("SBC") and its local exchange carrier subsidiaries filed a lawsuit in the United States District Court for the Northern District of Texas challenging on Constitutional grounds the Telecom Act restrictions applicable to the RBOCs only. The plaintiffs in the case seek both a declaratory judgment and an injunction against the enforcement of the challenged provisions. See "Business — Regulatory Overview."

On December 31, 1997, the United States District Court for the Northern District of Texas issued a decision holding that Sections 271 through 275, including the long distance entry provisions, of the Telecom Act are unconstitutional because they violate the separation of powers principles and bill of attainder provision of the U.S. Constitution. On February 11, 1998, the United States District Court for the Northern District of Texas granted the CLECs' request for a stay of the December 31, 1997 decision pending appeal to the United States Court of Appeals for the Fifth Circuit. That appeal is currently pending. If the stay is lifted, or if the Fifth Circuit upholds the district court's ruling, then the RBOCs would be free to enter the long distance market, providing additional competition to the Company's bundled service offering. In addition, the district court's ruling would eliminate the long distance entry incentives under the Telecom Act that were designed to promote interconnection between the ILEC and new competitors. The district court's decision has been appealed by the U.S. government and a number of other intervenors.

On May 8, 1997, the FCC released an order establishing a significantly expanded federal telecommunications subsidy regime which both increase the size of existing subsidies and created new subsidy funds. In the May 8 order, the FCC also announced that it will soon revise its rules for subsidizing service provided to consumers in high cost areas. The Company intends to make all subsidy payments required by law. See "Business — Regulatory Overview."

On July 18, 1997, the United States Court of Appeals for the Eighth Circuit overturned many of the rules the FCC had established pursuant to the Telecom Act governing the terms under which CLECs may, among other things, interconnect with ILECs, resell ILEC services, lease unbundled ILEC network elements and terminate traffic on ILEC networks. On October 14, 1997, the United States Court of Appeals for the Eighth Circuit vacated the FCC's rule prohibiting ILECs from separating unbundled network elements that are already combined, except at the request of the CLECs. These eighth Circuit decisions substantially limit the FCC's jurisdiction and expands the state regulators' jurisdiction to set and enforce rules governing the development of local competition. As a result, it is more likely that the rules governing local competition will vary substantially from state to state. Most states, however, have already begun to establish rules for local competition that are consistent with the FCC rules overturned by the Eighth Circuit. If a patchwork of state regulations were to develop, it could increase the Company's costs of regulatory compliance and could make competitive entry in some markets more difficult and expensive than in others. See "Business — Regulatory Overview."

Dependence on Large Customers

To date the Company has derived a substantial proportion of its revenues from certain large customers of its competitive access services and its IVR enhanced communication service offerings, the loss of one or more of which could have a material adverse effect on the Company's operating results. The Company's 10 largest customers accounted for approximately 25%, 51% and 66% of the Company's revenues in 1997, 1996 and 1995, respectively. The Company does not have long-term service contracts with most of these customers. The Company will continue to be dependent upon a small number of customers for a substantial portion of its revenues until such time, if at all, as the Company generates substantial revenues from the provision of switched local and long distance communications services.

Rapid Technological Changes; Licenses

The telecommunications industry is subject to rapid and significant changes in technology. The effect on the Company of technological changes, including changes relating to emerging wireline and wireless transmission and switching technologies, cannot be predicted. In addition, the Company from time to time receives requests to consider licensing certain patents held by third parties that may have bearing on its IVR and virtual communications center services. The Company considers such requests on their merits, but has not to date entered into any such license agreements. Should the Company be required to pay license fees in the future, such payments, if substantial, could have a material adverse effect on the Company's results of operations.

Dependence on Key Personnel

The Company's businesses are managed by a small number of key executive officers, the loss of certain of whom could have a material adverse effect on the Company. The Company believes that its future success will depend in large part on its ability to develop a large and sophisticated sales force and its ability to attract and retain highly skilled and qualified personnel. Most of the executive officers of the Company, including the presidents of its operating subsidiaries, do not have employment agreements. Although the Company has been successful in attracting and retaining qualified personnel, there can be no assurance that NEXTLINK will not experience a shortage of qualified personnel in the future.

Variability of Quarterly Operating Results

As a result of the significant expenses associated with the expansion and development of its networks and services and the variability of the level of revenues generated through sales of NEXTLINK's IVR enhanced communications services, the Company anticipates that its operating results could vary significantly from period to period.

Control by Mr. Craig O. McCaw; Potential Conflicts of Interests

Craig O. McCaw, primarily through his majority ownership and control of Eagle River Investments, L.L.C., a Washington limited liability company ("Eagle River"), controls approximately 52% of the Company's total voting power. As a result, Mr. McCaw has the ability to control the direction and future operations of the Company. Mr. McCaw is not an executive officer of the Company and, in addition to his investment in the Company through Eagle River, Mr. McCaw has significant investments in other communications companies, including Nextel Communications, Inc., Teledesic Corporation and Cable Plus Inc., some of which could compete with the Company as a single source provider of telecommunications services or act as a supplier to the Company of certain telecommunications services. The Company does not have a noncompetition agreement with either Mr. McCaw or Eagle River. Mr. McCaw is not bound by any contractual restrictions against sales of the Company's common stock.

Potential Volatility of Stock Price

The market price of the Company's common stock has been, and is likely to continue to be, volatile. The market price of the common stock could be subject to significant fluctuations in response to a number of factors, such as actual or anticipated variations in the Company's quarterly operating results, the introduction of new products by the Company or its competitors, changes in other conditions or trends in the Company's industry, changes in governmental regulations, changes in securities analysts' estimates of the Company's, or its competitors' or industry's, future performance or general market conditions. In addition, stock markets have experienced extreme price and volume volatility in recent years, which has had a substantial effect on the market prices of securities of many smaller public companies for reasons frequently unrelated to the operating performance of such companies.

Item 7. *Financial Statements and Supplementary Data*

The consolidated financial statements of the Company are filed under this Item, beginning on page 44 of this Report, and of NEXTLINK Capital are filed under this Item, beginning on Page 61 of this Report.

Item 8. *Changes in and Disagreements with Accountants on Accounting and Financial Disclosure*

None.

PART III

Item 9. *Directors and Executive Officers of the Company*

MANAGEMENT

The following table sets forth the names, ages and positions of the executive officers and members of the Company's board of directors. Their respective backgrounds are described following the table.

Name	Age	Position
Steven W. Hooper(3)	45	Chairman of the Board of Directors
Wayne M. Perry(1)	48	Vice Chairman and Chief Executive Officer
James F. Voelker(1)	47	President and Director
George M. Tronsrue III	41	Chief Operating Officer
Jan Loichle	50	Vice President, Chief of Local Exchange Operations
Kathleen H. Iskra	41	Vice President, Chief Financial Officer and Treasurer
R. Bruce Easter, Jr.	40	Vice President, General Counsel and Secretary
Charles P. Daniels	41	Vice President, Chief Technology Officer
Michael J. McHale, Jr.	41	Vice President, Chief Marketing Officer
R. Gerard Salemme	44	Vice President. External Affairs and Industry Relations
Craig O. McCaw	48	Director
Dennis Weibling(1)(2)(3)	46	Director
Scot Jarvis(2)	37	Director
William A. Hoglund(1)(2)	44	Director
Sharon L. Nelson(3)	51	Director
Jeffrey S. Raikes	39	Director

(1) Member of the Executive Committee

(2) Member of the Compensation Committee

(3) Member of the Audit Committee

The following persons are the presidents of the Company's operating subsidiaries:

Name	Age	Position
Hugh C. Cathey	47	President of NEXTLINK Ohio, L.L.C.
Don Hillenmeyer	52	President of NEXTLINK Tennessee, L.L.C.
Jeff C. Stone	40	President of NEXTLINK Interactive, L.L.C.
Dwayne Nielson	43	President of NEXTLINK Utah, L.L.C.
Gary Rawding	46	President of NEXTLINK Pennsylvania, L.P.
Donald W. Sessamen	64	President of NEXTLINK California, L.L.C.
Richard Kingston	38	President of NEXTLINK Illinois, Inc.

Directors of the Company are elected annually at the annual meeting of shareholders. The next annual meeting of shareholders is scheduled for May 1998. All of the officers identified above serve at the discretion of the Board of Directors of the Company. There are no family relationships between any person identified above.

The Audit Committee is responsible for reviewing the services provided by the Company's independent auditors, consulting with the independent auditors on audits and proposed audits of the Company and reviewing the need for internal auditing procedures and the adequacy of internal controls. The Compensation

Committee determines executive compensation and stock option awards. The Executive Committee exercises, to the maximum extent permitted by law, all powers of the Board of Directors between board meetings, except those functions assigned to specific committees. The Board of Directors may establish additional committees from time to time.

The following are brief biographies of persons identified above.

Steven W. Hooper. Mr. Hooper has been Chairman of the Board since July 21, 1997. Prior to that, Mr. Hooper was Vice Chairman of the Company since June 16, 1997. Mr. Hooper was formerly President and Chief Executive Officer of AT&T Wireless Services, Inc., following the merger with McCaw Cellular. Prior to being appointed President and Chief Executive Officer, he served as Chief Financial Officer for two years. This was preceded by five years as Regional President for Cellular One's Pacific Northwest/Rocky Mountain region, where his responsibilities included managing the cellular operations in six western states and Alaska. Mr. Hooper is a member of the Audit Committee of the Board of Directors.

Wayne M. Perry. Mr. Perry has been Chief Executive Officer of the Company since July 21, 1997 and Vice Chairman of the Company since June 16, 1997. Mr. Perry was formerly Vice Chairman of AT&T Wireless Services, Inc. since September 1994, following the merger with McCaw Cellular. Prior to the merger, he served as Vice Chairman of the Board of McCaw Cellular since June 1989, and before that served as President since December 1985. Prior to becoming President of McCaw Cellular, Mr. Perry served as Executive Vice President and General Counsel and was primary legal officer from 1976 to 1985. Mr. Perry was appointed Vice Chairman of the Board of LIN Broadcasting Corporation on March 5, 1990. He also served as Chairman of the Board of Directors of the Cellular Telecommunications Industry Association, the nationwide wireless industry association, for the 1993/94 term. Mr. Perry is a member of the Executive Committee of the Board of Directors.

James F. Voelker. Mr. Voelker has been the President of NEXTLINK since April 1995 and is responsible for developing the company vision and guiding overall operations. He is recognized as one of the early entrepreneurs in the business of building and delivering competitive local exchange service. Mr. Voelker's career in telecommunications spans almost two decades and includes experience in very different segments of the industry in a variety of executive positions. From 1981 to 1984 he served as Vice President of Sales, Marketing and Customer Service for Lexitel Corporation, the forerunner of Allnet Communications. Mr. Voelker co-founded Digital Signal Inc. and served as Chief Operating Officer and Chief Executive Officer from 1985 through the company's sale to SP Telecom in 1990. Digital Signal operated a nationwide fiber optic network supplying capacity, engineering, provisioning and operational support to over one hundred interexchange carriers. In the CAP arena, Mr. Voelker became Vice Chairman of City Signal Inc. in 1992, which constructed and operated networks in six markets. Subsequently, he served as its Chief Executive Officer after the company merged with its sister company Teledial America to form U.S. Signal. Based in Grand Rapids, Michigan, U.S. Signal was one of the first fully certified CLECs in the country. Mr. Voelker has served as Vice Chairman of ALTS, the industry Association of Local Telephone Service providers and as a director of Phoenix Network Inc., a publicly held long distance company. Mr. Voelker is also a member of the Executive Committee of the Board of Directors.

George M. Tronsrue III. Mr. Tronsrue has been Chief Operating Officer of NEXTLINK since October 1997. Prior to that, Mr. Tronsrue was part of the initial management team of ACSI from February 1994 to September 1997, and was responsible for planning and overseeing the operations of ACSI for its first three years serving as Chief Operating Officer, President, Strategy and Technology Development Division and Executive Vice President, Planning and Development. Prior to that, Mr. Tronsrue served as the Regional Vice President of the Central Region of Teleport Communications Group ("TCG"), and as Vice President, Emerging Markets overseeing the start-up of TCG's initial eight cable television partnerships. Before TCG, Mr. Tronsrue was at MFS Communications from its inception in 1987 until 1992. At MFS, Mr. Tronsrue served as Vice President, Corporate Planning and Information Management; Vice President, Field Sales; Vice President and General Manager for MFS New York during its first year of operations and Executive Vice President, MFS Internet. Prior to MFS, Mr. Tronsrue served at MCI from 1983 to 1986 in a variety of engineering and operations roles, culminating as Director of Operations, Michigan and Ohio.

Jan Loichle. Ms. Loichle has been Vice President, Chief of Local Exchange Operations of NEXTLINK since October 1996. Prior to that, Ms. Loichle was the President of NEXTLINK Solutions (the virtual communications center) from July 1995. Prior to joining NEXTLINK, Ms. Loichle was Executive Vice President at U.S. Signal in Detroit and Grand Rapids, Michigan from April 1993 to July 1995. At U.S. Signal Ms. Loichle led the development of an enhanced service platform (Magic Number) from concept through production system and implementation. From 1990 to 1993, Ms. Loichle was Assistant Vice President of Finance for SP Telecom in San Francisco. Prior to that, Ms. Loichle was Vice President of Financial Operations for Lexitel/Allnet/ALC in Birmingham, Michigan from December 1980 to October 1989.

Kathleen H. Iskra. Ms. Iskra has been Vice President, Chief Financial Officer and Treasurer of NEXTLINK since January 1996. Prior to that, she was President and Chief Executive Officer of Horizon Air, a wholly owned subsidiary of Alaska Air Group. Prior to her appointment at Horizon Air, Ms. Iskra served as staff Vice President of Finance and Controller of Alaska Airlines and Alaska Air Group. Ms. Iskra's service with Alaska began in 1987, when she was appointed Controller. Prior to joining Alaska, she was an audit manager with Arthur Andersen.

R. Bruce Easter, Jr. Mr. Easter has been Vice President, General Counsel and Secretary of NEXTLINK since January 1995. From 1986 to December 1994, Mr. Easter was an associate and then partner in the law firm of Davis Wright Tremaine in Seattle, Washington, where he focused on communications law and media matters.

Charles P. Daniels. Mr. Daniels has been Vice President, Chief Technology Officer since July 1997. Prior to that, Mr. Daniels was Vice President, Chief Marketing Officer of NEXTLINK from November 1995. From 1992 to 1995, Mr. Daniels worked for MCI where he was the founder and Program Manager of the network MCI Developers Lab. Mr. Daniels was also a founding member of MCI's Advanced Technology Group. Prior to joining MCI, Mr. Daniels worked for Manufacturers Hanover Trust from 1989 to 1992 as Vice President/Strategic Technology and Research, where he was responsible for evaluating and implementing new technologies that either reduced costs or generated new revenue.

Michael J. McHale, Jr. Mr. McHale has been Vice President, Chief Marketing Officer since November 1997. Prior to joining NEXTLINK, Mr. McHale served as Vice President and General Manager of the Phoenix market and Regional Vice President at Teleport Communications Group, Inc. from 1993, developing the Phoenix market from its inception. Prior to that, from 1991 to 1993, he was Vice President, Product Marketing and Development at MFS Intelenet, Inc. and was responsible for planning and implementing MFS's initial introduction of switched services in New York City.

R. Gerard Salemme. Mr. Salemme has been Vice President, External Affairs and Industry Relations since July 1997. Prior to joining NEXTLINK, Mr. Salemme was Vice President, Government Affairs at AT&T Corp. from December 1994. Prior to joining AT&T Corp., Mr. Salemme was Senior Vice President, External Affairs at McCaw Cellular from 1991 to December 1994.

Craig O. McCaw. Mr. McCaw has been a director of the Company since September 1994 and was Chief Executive Officer of NEXTLINK from September 1994 to July 21, 1997. Mr. McCaw is also Chairman and Chief Executive Officer of Eagle River, a company formed and owned by Mr. McCaw to make strategic investments in telecommunications ventures. Mr. McCaw was the founder, Chairman and Chief Executive Officer of McCaw Cellular, the nation's leading provider of wireless communications services, until the company was sold to AT&T in August 1994. Prior to entering the cellular telephone business in 1983, Mr. McCaw was requested by his family to assume responsibility for the daily operations of a small cable television operation in Centralia, Washington, that he and his three brothers owned. The one-system operation serving 4,000 subscribers eventually grew to be the nation's 20th largest cable operator serving 450,000 subscribers. In 1974, the cable company's services expanded by entering the paging and conventional mobile telephone industries. The company eventually became the fifth largest paging operator in the country, serving approximately 320,000 subscribers in 13 states. In 1981, the company began to develop broad-based cellular telephone services. Later, McCaw Cellular became the nation's largest cellular telephone operator, with cellular system positions in more than 100 U.S. cities, representing more than 100 million potential customers. The company also had interests in wireless data transmissions, personal communications services, air-to-ground phone systems and satellite communications at the time of its sale to AT&T. Mr. McCaw is one of the two principal owners of Teledesic Corporation, which in March 1994 announced plans for a worldwide satellite-based telecommunications system. Mr. McCaw is indirectly a significant stockholder, a director and Chairman of the Operating Committee of Nextel Communications, Inc., a provider of wireless telecommunications services. Mr. McCaw is also a director of Cable Plus, Inc.

Dennis Weibling. Mr. Weibling has been a director of the Company since January 1997 and had been Executive Vice President of NEXTLINK since September 1994. Mr. Weibling is also President of Eagle River, Inc., since October 1993. Mr. Weibling is a director and member of Nextel Communications, Inc.'s Board of Directors and operations, audit and compensation committees. Nextel is a leading provider of integrated wireless communications services for teams of mobile workers. Mr. Weibling serves on the board and executive committee of Teledesic Corporation, a satellite telecommunications company backed by Mr. McCaw and Microsoft founder Mr. William Gates. Mr. Weibling is a director of Cable Plus, one of the leading providers of private cable television and telephony service to residential apartment complexes. A licensed certified public accountant in Washington, Mr. Weibling is a member of the American Society of Certified Public Accountants and the Washington Society of Certified Public Accountants. In addition, Mr. Weibling is a licensed attorney in Ohio and a member of the American Bar Association and Ohio State Bar Association. Mr. Weibling is also a member of the Executive, Compensation and Audit Committees of the Board of Directors.

Scot Jarvis. Mr. Jarvis has been a director of the Company since January 1997 and, prior to that, had been Executive Vice President of NEXTLINK since September 1994, and was a Vice President of Eagle River, Inc. from October 1994 through April 1996. Mr. Jarvis is the co-founder and since March 1997 has been a member of Cedar Grove Partners, L.L.C. Prior to that, Mr. Jarvis was the acting President of the Company from September 1994 to April 1995. Prior to joining Eagle River, Inc., Mr. Jarvis served as Vice President of McCaw Development Corporation from 1993 to 1994 and of McCaw Cellular from 1985 through 1994. During his tenure at McCaw Cellular, Mr. Jarvis served in the positions of General Manager from 1990 to 1993, Vice President of Acquisitions and Development from 1988 to 1990 and Assistant Vice President from 1985 to 1988. Mr. Jarvis also recently served on the Board of Directors or executive committees of: NEXTEL Communications, Inc., PriCellular Corporation, Horizon Cellular Group, Los Angeles Cellular Telephone Company, Cellular 2000 Partnership, Cybertel Cellular Telephone Company (St. Louis), Northwest Cellular Partnership, and Movitel del Noroeste (Mexico Region). Mr. Jarvis has also served as the President of the Iberia Cellular Telephone Company from 1991 to 1994. Mr. Jarvis is also a member of the Compensation Committee of the Board of Directors.

William A. Hoglund. Mr. Hoglund has been a director of the Company since January 1997 and, prior to that, had been Executive Vice President of NEXTLINK since February 1996. Mr. Hoglund is also Vice President and Chief Financial Officer of Eagle River, Inc. since January 1996. Prior to joining Eagle River, Inc., Mr. Hoglund was Managing Director of J.P. Morgan & Co. in its investment banking group. Mr. Hoglund was employed by J.P. Morgan & Co. from 1977 through 1995, focusing for the past nine years on clients in the telecommunications, cable and media industries. Mr. Hoglund is also a member of the Executive and Compensation Committees of the Board of Directors.

Sharon L. Nelson. Ms. Nelson has been director of the Company since September 1997 and, prior to that, was Chairman of the Washington Utilities and Transportation Commission ("WUTC") from February 11, 1985 until her resignation on August 15, 1997. Prior to serving on the WUTC, Ms. Nelson served as staff coordinator for the Washington State Legislature's Joint Select Committee on Telecommunications (1983 to 1985), an attorney in private practice (1982 to 1983), legislative counsel to the Consumers Union of the United States (1978 to 1981), staff counsel to the Commerce Committee of the U.S. Senate (1976 to 1978) and secondary school teacher of history and anthropology (1969 to 1973). Ms. Nelson is also the past president of the National Association of Regulatory Utility Commissioners. Ms. Nelson also served on the Federal-State Joint Board on Universal Service created under the Telecom Act and as one of the 20-member negotiating team appointed by the Governors of Washington, Idaho, Oregon and Montana to review the Northwest electric power system. Ms. Nelson is also a member of the Audit Committee of the Board of Directors.

Jeffrey S. Raikes. Mr. Raikes has been a director of the Company since September 1997. He is also a member of the Executive Committee and the Group Vice President, Sales and Marketing of Microsoft Corporation. As Group Vice President, Mr. Raikes has responsibility for Microsoft's worldwide customer units as well as sales, marketing, support and service in the United States and Canada. Prior to joining the Executive Committee in July 1996, Mr. Raikes was Senior Vice President of Microsoft North America since 1993. Prior to serving as Senior Vice President of Microsoft North America, from 1990, Mr. Raikes was Vice President of Office Systems, where he was responsible for the development and marketing of word processing, workgroup applications and pen computing. From 1984 to 1990, Mr. Raikes was the Director of Applications Marketing, where he was the chief strategist behind Microsoft's graphical applications for the Apple Macintosh and Microsoft Windows as well as leading the product strategy and design of Microsoft Office. Mr. Raikes is also a member of the University of Nebraska Foundation and a Trustee of the Washington State University Foundation

The following individuals are the senior management of the Company's subsidiaries.

Hugh C. Cathey. Mr. Cathey has been the President of NEXTLINK Ohio since August 1996. Prior to joining NEXTLINK, Mr. Cathey had nearly 20 years of experience in the telecommunications industry. Mr. Cathey was President and Chief Executive Officer of Digital Network, Inc., a publicly traded, facilities-based long distance company based in Dallas, Texas. From 1989 to 1993, Mr. Cathey served as President and Chief Executive Officer of United Telemanagement, Inc. Prior to that, Mr. Cathey held sales and product management positions of increasing responsibility with AT&T, culminating as the senior executive of a business unit of AT&T with annual revenues of approximately $100 million. During Mr. Cathey's tenure at United Telemanagement, Inc., that company filed a petition under the Federal bankruptcy laws.

Don Hillenmeyer. Mr. Hillenmeyer has been the President of NEXTLINK Tennessee since March 1995. Prior to joining NEXTLINK in March of 1995, Mr. Hillenmeyer was president of MCMG, Inc., a Nashville-based wireless communications management consulting and operations firm specializing in running Rural Service Areas for independent cellular telephone owners. Before founding MCMG, Inc., Mr. Hillenmeyer held various senior management positions at McCaw Cellular and was responsible for 13 southern states from August 1986 to February 1990.

Jeff C. Stone. Mr. Stone has been the President of NEXTLINK Interactive (the IVR subsidiary) since August 1, 1997. Prior to joining the Company, Mr. Stone was Vice President and General Manager for the Western Region of WorldCom, Inc. (previously MFS Telecom, Inc.) from 1994 to July 1997. Prior to that, from 1989 to 1994, Mr. Stone was the Director of Sales and Marketing of Associated Communications of Los Angeles.

Dwayne Nielson. Mr. Nielson has been President of NEXTLINK Utah since February 1996. Prior to joining NEXTLINK, Mr. Nielson was Assistant Vice President, Consumer and Small Business Market, at Sprint Corporation from October 1994 to February 1996. Prior to that, from August 1985 through October 1994, Mr. Nielson held a variety of sales and marketing positions at Sprint and United Telephone.

Gary Rawding. Mr. Rawding has been President of NEXTLINK Pennsylvania since September 1994. Prior to founding Penns Light Communications, Inc., certain assets of which were acquired by the Company in September 1994, he served as Vice President of Sales and Marketing at Eastern TeleLogic Corporation from 1989 until 1993. Prior to joining Eastern TeleLogic, Mr. Rawding held various positions with Bell Atlantic Corporation.

Donald W. Sessamen. Mr. Sessamen has been President of NEXTLINK California since November 1996. Prior to that, Mr. Sessamen acted as a consultant to NEXTLINK. Prior to acting as a consultant to the Company, Mr. Sessamen joined Brooks Fiber California in 1994 as President, after the company acquired Phoenix Fiberlink. At Brooks Fiber California, Mr. Sessamen completed the installation of the San Jose system and managed the entry into switched services in the Sacramento market. From 1991 to 1994, Mr. Sessamen was Executive Vice President of Operations, Engineering and MIS at SP Telecom, a fiber optic systems construction and wholesale transmission company using Southern Pacific Railroad rights-of-way east of the Mississippi River. At SP Telecom, Mr. Sessamen led SP Telecom's entry into switch-based products utilizing the Northern Telecom DMS 250 Super Node, introducing innovative switch-based products.

Richard Kingston. Mr. Kingston has been the President of NEXTLINK Illinois since July 1997. Prior to joining NEXTLINK, Mr. Kingston was the Western Regional Vice President/General Manager of American Communications Services, Inc. from April 1994 to July 1997. Prior to that, Mr. Kingston operated his own telecommunications company, King Communications, Inc. from January 1992 to January 1994. From December 1990 to January 1992, Mr. Kingston was West Region Agent Manager for Telesphere Communications, Inc. and from 1988 to December 1990, Mr. Kingston was Director of Carrier Sales at MFS Communications Company, Inc.

Section 16(a) Beneficial Ownership Reporting Compliance

Information regarding compliance with Section 16(a) of the Securities Exchange Act of 1934 is set forth under the caption "Section 16(a) Beneficial Ownership Reporting Compliance" in the Company's Proxy Statement relating to the Company's annual meeting of shareholders to be held on May 20, 1998, and is incorporated herein by reference. Such Proxy Statement will be filed within 120 days of the Company's year end.

Item 10. *Executive Compensation*

Information called for by Part III, Item 10, is included in the Company's Proxy Statement relating to the Company's annual meeting of shareholders to be held on May 20, 1998, and is incorporated herein by reference. The information appears in the Proxy Statement under the caption "Compensation of Executive Officers." Such Proxy Statement will be filed within 120 days of the Company's year end.

Item 11. *Security Ownership of Certain Beneficial Owners and Management*

Information called for by Part III, Item 11, is included in the Company's Proxy Statement relating to the Company's annual meeting of shareholders to be held on May 20, 1998, and is incorporated herein by reference. The information appears in the Proxy Statement under the caption "Ownership of Certain Beneficial Owners." Such Proxy Statement will be filed within 120 days of the Company's year end.

Item 12. *Certain Relationships and Related Transactions*

Information called for by Part III, Item 12, is included in the Company's Proxy Statement relating to the Company's annual meeting of shareholders to be held on May 20, 1998, and is incorporated herein by reference. The information appears in the Proxy Statement under the caption "Certain Relationships and Related Transactions." Such Proxy Statement will be filed within 120 days of the Company's year end.

Item 13. *Exhibits, Financial Statement Schedules and Reports on Form 8-K*

(a) Financial Statements

NEXTLINK Communications, Inc.

NEXTLINK Capital, Inc.

(b) List of Exhibits:

Exhibit No.	Description
3.1	Articles of Incorporation of NEXTLINK Communications Inc.(2)
3.2	By-laws of NEXTLINK Communications, Inc.(2)
3.3	Articles of Incorporation of NEXTLINK Capital, Inc.(1)
3.4	By-laws of NEXTLINK Capital, Inc.(1)
4.1	Form of Exchange Note Indenture, by and among NEXTLINK Communications, Inc. and United States Trust Company of New York, as trustee, relating to the Exchange Notes, including form of Exchange Notes.(2)
4.2	Certificate of Designations of the Powers, Preferences and Relative, Participating, Optional and Other Special Rights of 14% Senior Exchangeable Redeemable Preferred Shares and Qualifications, Limitations and Restrictions Thereof.(2)
4.3	Form of stock certificate of 14% Senior Exchangeable Redeemable Preferred Shares.(2)
4.4	Indenture, dated as of April 25, 1996, by and among NEXTLINK Communications, Inc., NEXTLINK Capital, Inc. and United States Trust Company of New York, as Trustee, relating to 12½% Senior Notes due April 15, 2006, including form of global note.(1)
4.5	First Supplemental Indenture, dated as of January 31, 1997, by and among the Company, NEXTLINK Communications, L.L.C., NEXTLINK Capital and United States Trust Company of New York, as Trustee.(2)
4.6	Form of Indenture between United States Trust Company, as Trustee and NEXTLINK Communications, Inc., relating to the 9⅝% Senior Notes due 2007.(3)
4.7	Form of Indenture between United States Trust Company, as Trustee and NEXTLINK Communications, Inc., relating to the 9% Senior Notes Due 2008.
10.1	Stock Option Plan of the Company.(2)
10.2	First Amendment to Stock Option Plan of the Company.
10.3	Registration Rights Agreement dated as of January 15, 1997, between the Company and the signatories listed therein.(2)

Exhibit No.	Description
10.4	Preferred Exchange and Registration Rights Agreement, dated as of January 31, 1997, by and among the Company and the Initial Purchasers.(2)
10.5	Fiber Lease and Innerduct Use Agreement, dated as of February 23, 1998, by and between NEXTLINK Communications, Inc. and Metromedia Fiber Network, Inc.(4)
10.6	Amendment No. 1 to Fiber Lease and Innerduct Use Agreement, dated as of March 4, 1998, by and between NEXTLINK Communications, Inc. and Metromedia Fiber Network, Inc.(4)
21	Subsidiaries of the Registrants.
27.1	Financial Data Schedule for the year ended December 31, 1997.
27.2	Financial Data Schedule, restated for the periods ended December 31, 1996, June 30, 1997 and September 30, 1997.

(1) Incorporated herein by reference to the exhibit filed with the Registration Statement on Form S-4 of NEXTLINK Communications, L.L.C. (the predecessor of NEXTLINK Communications, Inc.) and NEXTLINK Capital, Inc. (Commission File No. 333-4603).

(2) Incorporated herein by reference to the exhibit filed with the Annual Report on Form 10-KSB for the year ended December 31, 1996 of NEXTLINK Communications, Inc. and NEXTLINK Capital, Inc. (Commission File Nos. 333-04603 and 333-04603-01).

(3) Incorporated herein by reference to the exhibit filed with the Registration Statement on Form S-1 of NEXTLINK Communications, Inc. (Commission File No. 333-32003).

(4) Portions of this exhibit were omitted and filed separately with the Secretary of the Commission pursuant to the Issuer's Application Requesting Confidential Treatment under Rule 24(b)-2 of the Securities Exchange Act of 1934.

(c) Reports on Form 8-K

None.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Board of Directors of NEXTLINK Communications, Inc.:

We have audited the accompanying consolidated balance sheets of NEXTLINK Communications, Inc. (a Washington Corporation) and subsidiaries as of December 31, 1997 and 1996, and the related consolidated statements of operations, changes in shareholders' equity (deficit) and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of NEXTLINK Communications, Inc. and subsidiaries as of December 31, 1997 and 1996, and the results of their operations and their cash flows for the years then ended in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Seattle, Washington,
March 12, 1998

NEXTLINK Communications, Inc.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share amounts)

ASSETS

	December 31, 1997	December 31, 1996
Current assets:		
Cash and cash equivalents	$ 389,074	$ 76,807
Marketable securities	353,283	47,713
Accounts receivable, net	22,955	7,008
Other	4,530	607
Pledged securities	41,425	39,770
Total current assets	811,267	171,905
Pledged securities	21,185	61,668
Property and equipment, net	253,653	97,784
Goodwill, net	52,278	24,110
Other assets, net	78,770	35,216
Total assets	$1,217,153	$390,683

LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)

	1997	1996
Current liabilities:		
Accounts payable	$ 26,776	$ 18,622
Accrued expenses	13,082	4,112
Notes payable	8,234	—
Accrued interest payable	18,880	9,250
Current portion of capital lease obligations	2,610	1,194
Payable to affiliate	—	1,500
Total current liabilities	69,582	34,678
Long-term debt	750,000	350,000
Capital lease obligations	7,640	6,262
Deferred compensation	—	10,289
Other long-term liabilities	3,179	2,850
Total liabilities	830,401	404,079
Commitments and contingencies		
Minority interests	23	308
Redeemable preferred stock (par value $0.01 per share, aggregate liquidation preference $323,478; 6,322,031 and 0 shares issued and outstanding in 1997 and 1996, respectively)	313,319	—
Class B common stock, subject to redemption (par value $0.02 per share, 519,950 and 0 shares issued and outstanding in 1997 and 1996, respectively)	4,950	—
Equity units subject to redemption (0 and 397,202 units outstanding in 1997 and 1996, respectively)	—	4,950
Shareholders' equity (deficit):		
Common stock, par value $0.02 per share, stated at amounts paid in; Class A, 110,334,000 shares authorized, 19,167,899 and 0 shares issued and outstanding in 1997 and 1996, respectively; Class B, 44,133,600 shares authorized, 33,746,573 and 0 shares issued and outstanding in 1997 and 1996, respectively	330,561	—
Deferred compensation	(9,596)	—
Accumulated deficit	(252,505)	(84,181)
Members' capital (28,154,509 units, all of which are outstanding in 1996)	—	65,527
Total shareholders' equity (deficit)	68,460	(18,654)
Total liabilities and shareholders' equity (deficit)	$1,217,153	$390,683

See accompanying notes to consolidated financial statements.

NEXTLINK Communications, Inc.

CONSOLIDATED STATEMENTS OF OPERATIONS
(Dollars in thousands, except per share amounts)

	Year Ended December 31, 1997	Year Ended December 31, 1996
Revenue	$ 57,579	$ 25,686
Costs and expenses:		
Operating	54,031	25,094
Selling, general and administrative	75,732	31,353
Deferred compensation	3,247	9,914
Depreciation	18,851	6,640
Amortization	8,339	3,700
Total costs and expenses	160,200	76,701
Loss from operations	(102,621)	(51,015)
Interest income	27,827	10,446
Interest expense	(54,495)	(30,876)
Loss before minority interests	(129,289)	(71,445)
Minority interests in loss of consolidated subsidiaries	285	344
Net loss	$ (129,004)	$ (71,101)
Preferred stock dividends and accretion of preferred stock redemption obligation, including issue costs	(39,320)	—
Net loss applicable to common shares	$ (168,324)	$ (71,101)
Pro forma:		
Net loss per share	$ (3.91)	$ (1.81)
Shares used in computation of pro forma net loss per share (1996 amounts have been adjusted for conversion of membership units into shares of the Company's Class A and Class B common stock upon incorporation; see Note 9)	43,055,885	39,312,482

See accompanying notes to consolidated financial statements.

NEXTLINK Communications, Inc.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (DEFICIT)

(Dollars in thousands)

	Common Stock						
	Shares						
	Class A	Class B	Amount	Deferred Compensation	Accumulated Deficit	Members' Capital	Total
Balance at December 31, 1995	—	—	$ —	$ —	$ (13,080)	$49,799	$ 36,719
Contributed capital	—	—	—	—	—	9,502	9,502
Issuance of units for NEXTLINK Ohio acquisition	—	—	—	—	—	652	652
Impact of recapitalization and merger of affiliates	—	—	—	—	—	5,574	5,574
Net loss	—	—	—	—	(71,101)	—	(71,101)
Balance at December 31, 1996	—	—	—	—	(84,181)	65,527	(18,654)
Merger of NEXTLINK Communications, L.L.C with and into NEXTLINK Communications, Inc.	—	36,165,259	65,527	—	—	(65,527)	—
Conversion of Equity Option Plan into Employee Stock Option Plan	—	—	15,363	(4,234)	—	—	11,129
Issuance of compensatory stock options	—	—	4,872	(4,872)	—	—	—
Compensation attributable to stock options vesting	—	—	—	2,335	—	—	2,335
Issuance of common stock under leasing arrangement	176,534	—	1,400	—	—	—	1,400
Issuance of common stock upon exercise of stock options	672,878	921,314	115	—	—	—	115
Issuance of common stock in initial public offering	14,280,000	—	226,760	—	—	—	226,760
Sale of common stock by selling shareholder in initial public offering	3,200,000	(3,200,000)	—	—	—	—	—
Issuance of common stock in acquisitions	698,487	—	16,524	—	—	—	16,524
Conversion of Class B common stock into Class A common stock	140,000	(140,000)	—	—	—	—	—
Loans to officers for income taxes paid upon exercise of stock options	—	—	—	(2,825)	—	—	(2,825)
Cumulative redeemable preferred stock dividends and accretion of preferred stock redemption obligation, including issue costs	—	—	—	—	(39,320)	—	(39,320)
Net loss	—	—	—	—	(129,004)	—	(129,004)
Balance at December 31, 1997	19,167,899	33,746,573	$330,561	$(9,596)	$(252,505)	$ —	$ 68,460

See accompanying notes to consolidated financial statements.

NEXTLINK Communications, Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands)

	Year Ended December 31, 1997	1996
OPERATING ACTIVITIES:		
Net loss	$(129,004)	$ (71,101)
Adjustments to reconcile net loss to net cash used in operating activities:		
Deferred compensation expense	3,247	9,914
Equity in loss of affiliates	2,544	1,100
Depreciation and amortization	27,190	10,340
Minority interests in loss of consolidated subsidiaries	(285)	(344)
Changes in assets and liabilities, net of effects from acquisitions:		
Accounts receivable	(11,206)	(1,659)
Other current assets	(1,953)	(42)
Other long-term assets	(1,208)	(1,430)
Accounts payable	4,116	993
Accrued expenses and other liabilities	2,434	2,416
Accrued interest payable	9,630	9,250
Net cash used in operating activities	(94,495)	(40,563)
INVESTING ACTIVITIES:		
Purchase of property and equipment	(142,170)	(51,920)
Investment in assets of acquired businesses (net of cash acquired)	(61,609)	(15,169)
Cash withdrawn from (placed into) escrow to be used in business acquisition	6,000	(6,000)
Investments in unconsolidated affiliates	(6,766)	(4,953)
Purchase of pledged securities	—	(117,688)
Maturity of pledged securities	39,920	16,431
Purchase of marketable securities, net	(305,570)	(47,713)
Net cash used in investing activities	(470,195)	(227,012)
FINANCING ACTIVITIES:		
Net proceeds from issuance of redeemable preferred stock	274,000	—
Capital contributions	—	9,935
Proceeds from payable to affiliates	—	28,766
Repayment of payable to affiliates	(1,500)	(33,703)
Repayment of capital lease obligations	(1,939)	(771)
Repayment of notes payable	(5,926)	—
Bank overdraft	—	(1,373)
Net proceeds from sale of common stock	226,760	—
Proceeds from sale of senior notes	400,000	350,000
Proceeds from issuance of common stock upon exercise of stock options	115	—
Costs incurred in connection with financing	(11,728)	(9,822)
Loans to officers for income taxes paid upon exercise of stock options	(2,825)	—
Net cash provided by financing activities	876,957	343,032
Net increase in cash and cash equivalents	312,267	75,457
Cash and cash equivalents, beginning of year	76,807	1,350
Cash and cash equivalents, end of year	$ 389,074	$ 76,807

See accompanying notes to consolidated financial statements.

NEXTLINK Communications, Inc.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 1997 and 1996

1. Organization and Description of Business

The consolidated financial statements include the accounts of NEXTLINK Communications, Inc., a Washington corporation, and its majority-owned subsidiaries (collectively referred to as the Company). The Company, through predecessor entities, was formed on September 16, 1994 and, through its subsidiaries, provides competitive local, long distance and enhanced telecommunications services in selected markets in the United States. The Company is a majority-owned subsidiary of Eagle River Investments, L.L.C. (Eagle River).

The competitive local telecommunications service business is a capital intensive business. The development of the Company's businesses and the installation and expansion of its networks require significant expenditures, a substantial portion of which must be made before any revenues may be realized. These expenditures, together with the associated early operating expenses, have resulted in negative cash flow and operating losses, which have been substantially financed with the proceeds from public sales of debt and equity securities.

2. Summary of Significant Accounting Policies

Principles of Consolidation

The Company's financial statements include 100% of the assets, liabilities and results of operations of subsidiaries in which the Company has a controlling interest of greater than 50%. The ownership interests of the other members or partners in such subsidiaries are reflected as minority interests. The Company's investment in Telecommunications of Nevada, L.L.C., (Nevada L.L.C.) a limited liability company in which the Company has a 40% interest and which operates a network that is managed by the Company in Las Vegas, Nevada, is accounted for on the equity method. Investments in entities in which the Company has voting interests of not more than 20% are accounted for on the cost method. All significant intercompany accounts and transactions have been eliminated.

Cash and Cash Equivalents

The Company considers all highly liquid investments with maturities of three months or less at the time of purchase to be cash equivalents.

Marketable Securities

Marketable securities consist of U.S. government and other securities with original maturities beyond three months. Marketable securities are stated at cost, adjusted for discount accretion and premium amortization. The securities in the Company's portfolio are classified as "held to maturity," as management has the intent and ability to hold those securities to maturity. The fair value of the Company's marketable securities approximates the carrying value.

Pledged Securities

In connection with the sale of 12½% Senior Notes (see Note 6), a portion of the net proceeds was utilized to purchase a portfolio consisting of U.S. government securities, which mature at dates sufficient to provide for payment in full of interest on the 12½% Senior Notes through April 15, 1999. The pledged securities are stated at cost, adjusted for premium amortization and accrued interest. The fair value of the pledged securities approximates the carrying value.

Property and Equipment

Property and equipment are stated at cost. Direct costs of construction are capitalized, including $1,793,000 and $853,000 of interest costs related to construction during 1997 and 1996, respectively. Depreciation is computed using the straight-line method over the estimated useful lives of the assets.

Estimated useful lives of property and equipment are as follows:

Telecommunications networks	5-20 years
Office equipment, furniture and other	3-5 years
Leasehold improvements	the lesser of the estimated useful lives or the terms of the leases

Intangible Assets

Intangible assets primarily represent costs allocated in acquisitions to customer bases and contracts, software and related intellectual property and goodwill. Intangible assets are amortized using the straight-line method over the estimated useful lives of the assets as follows:

Customer contracts	term of the contracts
Customer bases	5 years
Software and related intellectual property	5 years
Goodwill	15-20 years

Costs incurred in connection with securing the Company's debt facilities, including underwriting and advisory fees and other such costs, are deferred and amortized over the term of the financing using the straight-line method.

Income Taxes

Prior to January 31, 1997, the Company was organized and operated as a limited liability company that was classified and taxed as a partnership for federal and state income tax purposes. Effective February 1, 1997, the Company became subject to federal and state income taxes directly as a C corporation.

The Company accounts for income taxes in accordance with the provisions of Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (SFAS 109), which requires that deferred income taxes be determined based on the estimated future tax effects of differences between the financial statement and tax bases of assets and liabilities given the provisions of the enacted tax laws.

Revenue Recognition

The Company recognizes revenue on telecommunications and enhanced communications services in the period that services are provided.

Pro Forma Net Loss Per Share

Pro forma net loss per share has been computed using the number of shares of common stock and common stock equivalents outstanding. Pursuant to Securities and Exchange Commission Staff Accounting Bulletin No. 98 (SAB 98), issued in February 1998, nominal issuances of shares during the twelve-month period preceding the date of the initial filing of the Registration Statement have been included in the calculation of common stock equivalent shares as if such shares and options were outstanding for all periods presented. The provisions of SAB 98 require retroactive application; as such, pro forma net loss per share amounts and shares used in computation of pro forma net loss per share for all prior periods have been restated.

In February 1997, the Financial Accounting Standards Board issued Statement No. 128, "Earnings Per Share" (SFAS 128), which revises the calculation and presentation provisions of Accounting Principles Board (APB) Opinion No. 15 and related interpretations. SFAS 128 is effective for the Company's fiscal year ending December 31, 1997, and retroactive application is required. Implementation of SFAS 128 did not have a material effect on the Company's earnings per share amounts reported prior to that date.

Stock-Based Compensation

As allowed by Statement No. 123, "Accounting for Stock-Based Compensation" (SFAS 123), the Company has chosen to account for compensation cost associated with its stock option plans in accordance with APB Opinion No. 25.

Concentration of Credit Risk

Financial instruments which potentially subject the Company to concentrations of credit risk consist primarily of trade receivables. The Company's trade receivables are geographically dispersed and include customers in many different industries. Management believes that any risk of loss is significantly reduced due to the diversity of its customers and geographic sales areas. The Company continually evaluates the creditworthiness of its customers; however, it generally does not require collateral. The Company's allowance for doubtful accounts is based on historical trends, current market conditions and other relevant factors.

Use of Estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to prior period amounts in order to conform to the current year presentation.

3. Acquisitions

On November 1, 1997, the Company acquired all of the outstanding shares of Start Technologies Corporation (Start), a shared tenant services provider offering local and long distance services, Internet access and customer premise equipment management in Texas and Arizona. The Company paid consideration for the transaction consisting of $20.0 million in cash, 441,336 shares of Class A common stock, and the assumption of approximately $5.3 million of liabilities, the majority of which were repaid.

On October 1, 1997, the Company acquired all of the outstanding shares of Chadwick Telecommunications Corporation (Chadwick), a switch-based long distance reseller in central Pennsylvania, through a merger transaction between Chadwick and a wholly owned subsidiary of the Company. The purchase price of the transaction consisted of a $5.0 million promissory note payable, due January 1, 1998, issuance of 257,151 shares of Class A common stock, and the repayment of long-term debt and other liabilities totaling $6.6 million. The merger agreement also provides for additional payments of up to a maximum of 192,863 shares of Class A common stock over a two-year period, with these payments being contingent upon the acquired operation achieving specified performance goals.

On February 4, 1997, the Company acquired substantially all of the assets of Linkatel Pacific, L.P. (Linkatel), a Los Angeles-based competitive access telecommunications provider. At the time of the acquisition, Linkatel operated an 80 mile fiber optic telecommunications network covering several markets from the downtown Los Angeles area to the city of Irvine in Orange County. As part of the assets acquired, the Company obtained access to approximately 250 route miles of right-of-way, of which 183 miles have been completed, creating one network in Los Angeles and one network in the Orange County area. The Company has been providing competitive access services over these networks since the acquisition date and launched switched local and long distance services in July 1997. The total purchase price of $42.5 million consisted of a cash payment of $36.1 million, the repayment of debt of $5.6 million and the assumption of net liabilities of $0.8 million.

In December 1996, the Company acquired ITC, a switched-based long distance reseller based in Salt Lake City, Utah. Consideration for the acquisition of ITC consisted of a cash payment of $4.0 million, of which $2.6 million was placed into escrow to be paid during 1998, plus the issuance of 397,202 Class A Units of the Company valued at approximately $5.0 million, which were subsequently converted into 519,950 shares of the Company's Class B common stock. The Company has granted the seller an option requiring the Company to repurchase such shares at $19.92 per share beginning in the fourth quarter of 1999. This repurchase obligation will terminate if during the three-year period commencing March 25, 1998, the average daily closing price of the Class A common stock during any consecutive 60 trading day period is greater than $19.92.

In January 1996, the Company acquired certain assets of FoneNet, Inc. and U.S. Network, Inc. through NEXTLINK Ohio, L.L.C. Consideration for the purchase consisted of a cash payment of $9.6 million, the issuance of 287,721 Class A Units of the Company, valued at $651,933, plus the assumption of capital lease obligations of $6.1 million.

The above acquisitions were accounted for using the purchase method of accounting and, accordingly, the results of operations of the acquired companies have been included in the Company's consolidated financial statements since the effective dates of acquisition. The aggregate purchase price for the acquisitions occurring in 1997 and 1996 were allocated based on fair values as follows (in thousands):

	1997	1996
Fair value of tangible assets acquired and liabilities assumed	$12,525	$12,579
Fair value of intangible assets acquired	70,705	16,425
	$83,230	$29,004
Purchase price	$83,230	$29,004

The following unaudited condensed pro forma information presents the results of operations of the Company for the years ended December 31, 1997 and 1996 as if the above transactions had occurred on January 1, 1996 (in thousands, except per share amounts):

	1997	1996
Revenue	$ 79,070	$ 58,050
Net loss	$(134,404)	$(74,423)
Net loss per share	$ (3.12)	$ (1.89)

The unaudited pro forma information is provided for informational purposes only and is not necessarily indicative of the results of operations that would have occurred had the purchases been made on January 1, 1996, or of the future anticipated results of operations of the combined companies.

4. Property and Equipment

Property and equipment consisted of the following components (in thousands):

	December 31,	
	1997	1996
Telecommunications networks	$189,629	$66,762
Office equipment, leasehold improvements, furniture and other	38,979	18,097
	228,608	84,859
Less accumulated depreciation	36,417	8,369
	192,191	76,490
Network construction in progress	61,462	21,294
	$253,653	$97,784

In June 1997, the Company entered into an eight-year operating lease agreement, with an option to renew for five additional years, with a company that has excess fiber capacity in Atlanta, Chicago, New York City, Newark, New Jersey, and Philadelphia which it agreed to make available to the Company in each of those markets. Payment in exchange for use of the leased network will be based on monthly charges for actual services provided. In connection with this lease agreement, the Company also issued to the lessor 176,534 shares of Class A common stock in June 1997 for certain exclusivity rights to the excess capacity.

In addition to the capacity arrangement described above, in June 1997, the Company entered into a 20-year capital lease over an existing 47-mile fiber network in New York City. In connection with this arrangement, the Company paid $11 million in full satisfaction of its obligation under the lease, $6 million of which was placed in escrow pending completion of certain building connections by the lessor. As of December 31, 1997, $4.1 million remained in escrow.

5. Other Assets

Other assets consisted of the following components (in thousands):

	December 31,	
	1997	1996
Customer bases	$53,033	$12,003
Equity investments	8,021	3,853
Financing costs	21,552	9,822
Cash held in escrow for acquisitions	—	8,682
Advances to business to be acquired	—	1,490
Other noncurrent assets	8,415	4,627
	91,021	40,477
Less accumulated amortization	12,251	5,261
	$78,770	$35,216

The Company's equity investments include (i) a 40% investment in Nevada L.L.C., which operates a fiber optic telecommunications network serving the Las Vegas market and (ii) a $3.7 million investment in convertible preferred stock of Intermind Corporation (Intermind). Intermind has developed and patented an interactive communications tool for the World Wide Web and intranet applications.

6. Long-Term Debt

On October 1, 1997, the Company sold $400 million in aggregate principal amount of 9⅝% Senior Notes due October 1, 2007, which, after deducting issue costs, resulted in net proceeds to the Company of $388.5 million. Interest payments on the 9⅝% Senior Notes are due semi-annually. The 9⅝% Senior Notes are redeemable at the option of the Company, in whole or in part, at any time on or after October 1, 2002 at established redemption prices which decline to 100% of the stated principal amount thereof by October 1, 2005.

On April 25, 1996, the Company completed the sale and issuance of $350 million in principal amount of 12½% Senior Notes due April 15, 2006. The Company used $117.7 million of the gross proceeds to purchase U.S. government securities, representing funds sufficient to provide for payment in full of interest on the 12½% Senior Notes through April 15, 1999 and used an additional $32.2 million to repay advances and accrued interest from Eagle River. In addition, the Company incurred costs of $9.8 million in connection with the financing (including underwriter discounts and commissions). Interest payments on the 12½% Senior Notes are due semi-annually. The 12½% Senior Notes are redeemable at the option of the Company, in whole or in part, at any time on or after April 15, 2001 at established redemption prices which decline to 100% of the stated principal amount thereof by April 15, 2004. As of December 31, 1997, the approximate fair value of the 12½% Senior Notes was $402.5 million, based on quoted market prices.

The indentures pursuant to which the 9⅝% and 12½% Senior Notes (the Notes) are issued contain certain covenants that, among other things, limit the ability of the Company and its subsidiaries to incur additional indebtedness, issue stock in subsidiaries, pay dividends or make other distributions, repurchase equity interests or subordinated indebtedness, engage in sale and leaseback transactions, create certain liens, enter into certain transactions with affiliates, sell assets of the Company and its subsidiaries, and enter into certain mergers and consolidations.

In the event of a change in control of the Company as defined in the indentures, holders of the Notes will have the right to require the Company to purchase their Notes, in whole or in part, at a price equal to 101% of the stated principal amount thereof, plus accrued and unpaid interest, if any, thereon to the date of purchase. The Notes are senior unsecured obligations of the Company, and are subordinated to all current and future indebtedness of the Company's subsidiaries, including trade payables.

7. Redeemable Preferred Stock

On January 31, 1997, the Company completed the sale of 5.7 million units consisting of (i) 14% senior exchangeable redeemable preferred shares (Preferred Shares), liquidation preference $50 per share, and (ii) contingent warrants to acquire in the aggregate 5% of each class of outstanding junior shares (as defined) of the Company on a fully diluted basis as of February 1, 1998, which resulted in gross proceeds to the Company of $285 million, and proceeds net of underwriting discounts, advisory fees and expenses of $274 million. The contingent warrants expired unused on October 31, 1997 (30 days after the Company's initial public offering of its Class A common stock). Dividends on the Preferred Shares accrue from January 31, 1997 and are payable quarterly, commencing on May 1, 1997, at an annual rate of 14% of the liquidation preference thereof. Dividends may be paid, at the Company's option, on any dividend payment date occurring on or prior to February 1, 2002, either in cash or by issuing additional Preferred Shares with an aggregate liquidation preference equal to the amount of such dividends. The Company is required to redeem all of the Preferred Shares outstanding on February 1, 2009 at a redemption price equal to 100% of the liquidation preference thereof, plus accumulated and unpaid dividends to the date of redemption. As of December 31, 1997, the approximate fair value of the Preferred Shares was $345.1 million, based on quoted market prices.

Subject to certain conditions and the modifications of covenants, the Preferred Shares are exchangeable in whole, but not in part, at the option of the Company, on any dividend payment date, for 14% senior subordinated notes (Senior Subordinated Notes) due February 1, 2009 of the Company. All terms and conditions (other than interest, ranking and maturity) of the Senior Subordinated Notes would be substantially the same as those of the Company's outstanding 12½% Senior Notes due April 15, 2006.

8. Income Taxes

Prior to January 31, 1997, the Company was organized and operated as a limited liability company that was classified and taxed as a partnership for federal and state income tax purposes. Effective February 1, 1997, the Company became subject to federal and state income taxes directly as a C corporation, which resulted in the Company recording a deferred tax liability and deferred tax provision at that time.

Components of deferred tax assets and liabilities as of February 1, 1997 (date of conversion to a C corporation) and December 31, 1997 are as follows (in thousands):

	February 1, 1997	December 31, 1997
Deferred tax assets:		
Amortization	$ 994	$ 1,116
Capitalized costs	4,076	6,508
Provisions not currently deductible	252	1,191
Net operating loss carryforwards	—	47,734
Total deferred tax assets	5,322	56,549
Valuation allowance	—	(34,064)
	5,322	22,485
Deferred tax liabilities:		
Depreciation	(705)	(1,499)
Purchase acquisitions	(6,458)	(20,374)
Other	(686)	(612)
Total deferred tax liabilities	(7,849)	(22,485)
Net deferred taxes	$(2,527)	$ —

During 1997, the valuation allowance increased $34.1 million, thereby fully reserving the Company's net deferred tax assets as of December 31, 1997.

As of December 31, 1997, the Company had net operating loss carryforwards of approximately $119.3 million, which are available to offset future federal and state taxable income, if any, through 2012.

A reconciliation of the Company's effective income tax rate and the U.S. federal tax rate is as follows:

	Year Ended December 31, 1997
Statutory rate	34.0%
State income taxes, net of federal benefit	6.0%
Conversion to C corporation	(1.9%)
Valuation allowance for deferred tax assets	(26.1%)
Purchase acquisitions	(12.0%)
	—%

9. Shareholders' Equity (Deficit)

On October 1, 1997, the Company completed an initial public offering (IPO) of 12,000,000 shares of Class A common stock at a price of $17 per share. In addition, the underwriters of the IPO exercised an option to purchase 2,280,000 additional shares of Class A common stock at the same price per share. Gross proceeds from the IPO totaled approximately $242.8 million, and proceeds net of underwriting discounts, advisory fees and expenses aggregated approximately $226.8 million.

On August 27, 1997, the Company effected a 0.441336-for-1 reverse stock split of the issued and outstanding shares of Class A and Class B common stock. All common stock, membership units, and per share amounts in the consolidated financial statements have been adjusted retroactively to give effect to the reverse stock split.

From January 31, 1997, the Company had two classes of common stock outstanding, Class A common stock and Class B common stock. The Company's Class A common stock and Class B common stock are identical in dividend and liquidation rights, and vote together as a single class on all matters, except as otherwise required by applicable law, with the Class A shareholders entitled to cast one vote per share, and the Class B shareholders entitled to cast 10 votes per share.

On January 31, 1997, NEXTLINK Communications, L.L.C. was merged with and into the Company in a tax-free transaction. In that merger, the Class A membership interests of NEXTLINK Communications, L.L.C. were converted into Class B common stock, options to acquire Class A membership interests were converted into options to purchase Class B common stock, and options to purchase Class B membership interests were converted into options to purchase Class A common stock. In calculating the number of shares of the Company's Class B common stock that each of the Class A members received in the merger, the Company applied a formula that reflected each member's revalued capital account balance as of January 31, 1997. Options to purchase Class B membership interests were converted into the right to receive options to purchase shares of Class A common stock on a one to one basis.

Prior to January 31, 1997, the Company's limited liability company agreement provided for both Class A and Class B membership interests in the Company. Class A Unit holders were entitled to a preferred return on their investment in the Company plus a return of their capital upon the dissolution of the Company. Class B Units were granted in connection with the Company's Amended and Restated Equity Option Plan (EOP). Although Class B Units, when exercised, constituted an ownership interest in the Company, the interest was limited to the appreciation in the value of the Company, or the distributable profits interest, if any, of the Company. The valuation of the membership units was determined by the EOP Administrative Committee. As of December 31, 1996, the value of the Class A Units was determined to be approximately $9.88, and the appreciation interest per unit for Class B Units was approximately $7.93.

Effective January 1, 1996, the Company merged four of its five operating subsidiaries with newly formed entities owned by the Company. As a result of these mergers, the entities and individuals holding minority interests in the subsidiaries exchanged these interests for 1,695,263 Class A Units of the Company (representing an approximate 5.9% ownership interest in the Company) which were valued at approximately $5.6 million. NEXTLINK Washington, L.L.C. did not participate in the merger. The transaction was accounted for as a purchase of minority interests. Accordingly, the $2.9 million excess of the purchase price over the book value of the interests acquired was recorded as goodwill.

In addition to the exchange of equity interests, the Company exchanged options to acquire equity interests in the subsidiaries for options to acquire Class B Units in the Company. In connection with this transaction, the Company issued 862,219 options with exercise prices of $0.02 and four-year vesting schedules. These options had substantially the same economic values and vesting schedules as the subsidiary options which were exchanged.

10. Pro Forma Net Loss Per Share

Shares used in the computation of net loss per share amounts were calculated as follows:

	1997	1996
Weighted average common shares outstanding	41,144,275	36,208,588
Nominal issuances during the 12 month period prior to the Company's filing of its IPO, treated as if outstanding for all periods presented	1,911,610	3,103,894
Shares used in computation of pro forma net loss per share	43,055,885	39,312,482

Subsequent to the Company's IPO and through December 31, 1997, options to purchase 307,164 shares of common stock were issued but were not included in the computation of net loss per share, as these options did not fall under the provisions of SAB 98 and inclusion of such options would have been antidilutive.

11. Stock Options

Prior to February 1997, the Company maintained an Equity Option Plan which provided for the granting of equity option interests in the Company. These option grants were considered compensatory and were accounted for similarly to stock appreciation rights. The Company recognized compensation expense over the vesting periods based on the excess of the fair value of the equity option interests, as determined by the Administrative Committee, over the exercise price of the option interests. Such expense was periodically adjusted for changes in the fair value of the equity interest units. These option interests vested ratably over a four-year period, although some retained vesting schedules of previous option plans which, in most cases, vested 20% at employment and 20% at the end of each subsequent year.

In connection with the incorporation of the Company (see Note 9), the Company established the NEXTLINK Communications, Inc. Stock Option Plan (the Plan) to replace the Equity Option Plan and to provide a performance incentive for certain officers, employees and individuals or companies who provide services to the Company. The Plan provides for the granting of qualified and non-qualified stock options. All options outstanding under the Equity Option Plan were regranted under the new Plan with terms and conditions substantially the same as under the Equity Option Plan, except that option holders will no longer have the option to require the Company to repurchase units for cash upon exercise of such units, nor will the Company have the option to repurchase exercised units for cash. The Company has reserved 4,413,360 shares of Class A common stock for issuance under the Plan. The options generally vest ratably over four years and expire no later than 10 years after the date of grant, with the exception of options originally granted under the Equity Option Plan, which expire 15 years after the date of grant.

The exercise price of qualified stock options granted under the Plan may not be less than the fair market value of the common shares on the date of grant. The exercise price of non-qualified stock options granted under the Plan may be greater or less than the fair market value of the common stock on the date of grant, as determined at the discretion of the Board of Directors. Stock options granted at prices below fair market value at the date of grant are considered compensatory, and compensation expense is deferred and recognized ratably over the option vesting period based on the excess of the fair market value of the stock at the date of grant over the exercise price of the option. In connection with the regranting of options under the new Plan, the Company reclassified the deferred compensation liability relating to compensatory options issued under the Equity Option Plan to common stock, stated at amounts paid in. The remaining, unrecognized compensation expense attributable to these compensatory options was also recorded as deferred compensation, a contra-equity balance, and will be recognized over the remaining vesting periods of the options.

During 1997, the Company recorded approximately $2,355,000 and $892,000 of deferred compensation expense related to the Stock Option Plan and Equity Option Plan, respectively. For the year ended December 31, 1996, the Company recorded approximately $9,914,000 of deferred compensation expense related to the Equity Option Plan.

The Company has adopted the disclosure-only provisions of SFAS 123. Had compensation costs been recognized based on the fair value at the date of grant for options awarded under the Plans, the pro forma amounts of the Company's net loss and net loss per share for the years ended December 31, 1997 and 1996 would have been as follows (in thousands, except per share amounts):

	1997	1996
Net loss applicable to common shares — as reported	$(168,324)	$(71,101)
Net loss applicable to common shares — pro forma	$(182,571)	$(64,512)
Net loss per share — as reported	$ (3.91)	$ (1.81)
Net loss per share — pro forma	$ (4.24)	$ (1.64)

The fair value of each option grant was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions: risk-free interest rates of 5.31% to 7.05%; expected option lives of 3 to 5 years; expected volatility of 45%; and no expected dividends. The weighted average fair value of options granted during 1997 and 1996 was $5.94 and $6.87, respectively.

Information with respect to the Equity Option Plan and Stock Option Plan is as follows:

	Shares Subject to Option	Option Price Range	Weighted Average Exercise Price
Options outstanding at December 31, 1995	1,594,471	$0.02	$0.02
Granted	455,018	$0.02 - 7.93	$1.93
Canceled	(44,843)	$0.02	$0.02
Options outstanding at December 31, 1996	2,004,646	$0.02 - 7.93	$0.45
Granted	2,569,156	$7.93 - 26.50	$9.24
Canceled	(205,398)	$0.02 - 21.31	$1.19
Exercised	(672,878)	$0.02 - 7.93	$0.18
Options outstanding at December 31, 1997	3,695,526	$0.02 - 26.50	$6.45

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Options Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Options Exercisable	Weighted Average Exercise Price
$ 0.02 - $ 1.00	1,146,886	12.54	$ 0.23	411,470	$ 0.10
$ 1.01 - $14.00	2,289,755	10.82	$ 7.95	103,256	$ 7.93
$14.01 - $26.50	258,885	9.92	$20.53	110,308	$21.94

At December 31, 1997, 44,956 shares of Class A common stock were available for future grants. The Board of Directors has authorized an increase of 5,441,336 in the number of shares that may be issued pursuant to options under the Plan, subject to shareholder approval. The Company has received an irrevocable proxy from its majority shareholder approving the increase.

12. Supplemental Disclosure of Cash Flow Information

Supplemental disclosure of the Company's cash flow information is as follows (in thousands):

	Year Ended December 31, 1997	1996
Noncash financing and investing activities were as follows:		
Class A common stock issued under lease arrangement	$ 1,400	$ —
Redeemable preferred stock dividends, paid in redeemable preferred shares	$31,102	$ —
Accrued redeemable preferred stock dividends, payable in redeemable preferred shares, and accretion of preferred stock redemption obligation	$ 8,218	$ —
Issuance of notes payable and assumption of liabilities in acquisitions	$21,280	$ 8,228
Issuance of Class A common stock in acquisitions	$16,524	$ —
Capital lease obligations assumed	$ 4,725	$ 1,377
Members' equity recorded in Recapitalization	$ —	$ 5,574
Goodwill recorded in Recapitalization	$ —	$ 2,907
Exchange of minority interests for Class A units	$ —	$ 2,667
Cash paid for interest	$44,865	$20,912

13. Commitments and Contingencies

Capitalized leases consist of leases of telecommunications equipment and fiber optic networks. The Company is also leasing premises under various operating leases which, in addition to rental payments, require payments for insurance, maintenance, property taxes and other executory costs related to the leases. The lease agreements have various expiration dates and renewal options through 2028.

Future minimum payments required under capital and operating leases that have an initial or remaining noncancelable lease term in excess of one year at December 31, 1997 were as follows (in thousands):

	Capital Leases	Operating Leases
Year ending December 31,		
1998	$ 3,285	$ 7,005
1999	3,199	7,269
2000	2,825	6,950
2001	1,209	6,461
2002	1,205	6,305
Thereafter	5,174	22,695
Total minimum lease payments	16,897	
Less amounts representing interest	6,647	
Present value of future minimum lease payments	10,250	
Less amounts due in one year	2,610	
	$ 7,640	

Rent expense totaled approximately $6,376,000 and $2,248,000 in 1997 and 1996, respectively.

14. SUBSEQUENT EVENTS

Joint Venture

In January 1998, the Company and Nextel Communications, Inc. (Nextel) formed a joint venture called NEXTBAND Communications, L.L.C. (NEXTBAND), which is owned 50% each by the Company and Nextel. On January 28, 1998, NEXTBAND filed an application with the FCC for which it paid a $50 million refundable deposit to participate in the FCC's Local Multipoint Distribution Service (LMDS) auction which began on February 18, 1998. Of the deposit amount, $25 million was deposited by the Company. LMDS is a fixed broadband point-to-multipoint service which the FCC and industry analysts anticipate will be used for the deployment of wireless local loop, high-speed data transfer and video broadcasting service. NEXTBAND has applied for and is eligible to bid on any of the markets being auctioned for the licenses, which could result in additional funds being contributed by the Company to NEXTBAND.

Network Lease

In February 1998, the Company entered into a 20-year capital lease for exclusive rights to multiple fibers and innerducts extending over 650 route miles throughout New York, New Jersey, Connecticut, Pennsylvania, Delaware, Maryland and Washington, D.C. The Company paid $92.0 million for the transaction, of which $80.3 million was placed into escrow pending completion and delivery of segments of the network route to the Company. The Company has the option to renew the lease for two additional 10-year terms.

Financing

On March 3, 1998, the Company completed the sale of $335 million in aggregate principal amount of 9% Senior Notes due March 15, 2008. Proceeds from the sale net of discounts, underwriting commissions, advisory fees and expenses, totaled approximately $326.5 million. The 9% Senior Notes are redeemable at the option of the Company, in whole or in part, beginning March 15, 2003 at established redemption prices which decline to 100% of the stated principal amount thereof by March 15, 2006.

The indenture pursuant to which the 9% Senior Notes are issued contains certain covenants that, among other things, limits the ability of the Company and its subsidiaries to incur additional indebtedness, issue stock in subsidiaries, pay dividends or make other distributions, repurchase equity interests or subordinated indebtedness, engage in sale and leaseback transactions, create certain liens, enter into certain transactions with affiliates, sell assets of the Company and its subsidiaries, and enter into certain mergers and consolidations.

In the event of a change in control of the Company as defined in the indenture, holders of the 9% Senior Notes will have the right to require the Company to purchase their 9% Senior Notes, in whole or in part, at a price equal to 101% of the stated principal amount thereof, plus accrued and unpaid interest, if any, thereon to the date of purchase. The 9% Senior Notes are senior unsecured obligations of the Company, and are subordinated to all current and future indebtedness of the Company's subsidiaries, including trade payables.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To NEXTLINK Capital, Inc.:

We have audited the accompanying balance sheets of NEXTLINK Capital, Inc. (a Washington corporation) as of December 31, 1997 and 1996. These balance sheets are the responsibility of the Company's management. Our responsibility is to express an opinion on these balance sheets based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the balance sheets are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the balance sheets. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the balance sheets referred to above present fairly, in all material respects, the financial position of NEXTLINK Capital, Inc. as of December 31, 1997 and 1996 in conformity with generally accepted accounting principles.

ARTHUR ANDERSEN LLP

Seattle, Washington,
March 12, 1998

NEXTLINK Capital, Inc.

BALANCE SHEETS

ASSETS

	December 31, 1997	December 31, 1996
Cash in bank	$100	$100

SHAREHOLDER'S EQUITY

Common stock, no par value, 1,000 shares authorized, issued and outstanding	$100	$100

See accompanying note to balance sheets.

NEXTLINK Capital, Inc.

NOTE TO BALANCE SHEETS
December 31, 1997 and 1996

1. Description

NEXTLINK Capital, Inc. (NEXTLINK Capital) is a Washington corporation and a wholly owned subsidiary of NEXTLINK Communications, Inc. (NEXTLINK). NEXTLINK Capital was formed for the sole purpose of obtaining financing from external sources and is a joint obligor on the 12½% Senior Notes due April 15, 2006 of NEXTLINK. NEXTLINK Capital was initially funded with a $100 contribution from NEXTLINK and has had no operations to date. NEXTLINK Capital's sole source and repayment for the 12½% Senior Notes will be from the operations of NEXTLINK. Therefore, these balance sheets should be read in conjunction with the consolidated financial statements of NEXTLINK.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrants have duly caused this report to be signed on their behalf by the undersigned thereunto duly authorized.

NEXTLINK Communications, Inc.

Date: March 25, 1998

By: /s/ WAYNE M. PERRY
Wayne M. Perry
Chief Executive Officer, Director

NEXTLINK Capital, Inc.

Date: March 25, 1998

By: /s/ WAYNE M. PERRY
Wayne M. Perry
Chief Executive Officer, Director

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on March 25, 1998 by the following persons on behalf of the Registrants and in the capacities indicated:

Name	Title
/s/ WAYNE M. PERRY Wayne M. Perry	Chief Executive Officer, Director
/s/ KATHLEEN H. ISKRA Kathleen H. Iskra	Vice President, Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)
/s/ JAMES F. VOELKER James F. Voelker	President, Director (Principal Executive Officer)
/s/ STEVEN W. HOOPER Steven W. Hooper	Director
/s/ CRAIG O. McCAW Craig O. McCaw	Director
/s/ DENNIS WEIBLING Dennis Weibling	Director
/s/ SCOT JARVIS Scot Jarvis	Director
/s/ WILLIAM A. HOGLUND William A. Hoglund	Director
/s/ SHARON L. NELSON Sharon L. Nelson	Director
/s/ JEFFREY S. RAIKES Jeffrey S. Raikes	Director

Exh. E

FLORIDA TELECOMMUNICATIONS TARIFF

This tariff contains the descriptions, regulations and rates applicable to the furnishing of service and facilities for telecommunications services provided by NEXTLINK Long Distance Service, Inc. with principal offices at 508 108th Avenue N.E., Suite 2200, Bellevue, Washington 98004. This tariff applies for services furnished within the **State of Florida**. This tariff is on file with the Florida Public Service Commission, and copies may be inspected during normal business hours at the Company's principal place of business.

Douglas W. Kinkoph, Vice President
NEXTLINK Long Distance Services, Inc.
Two Easton Oval
Columbus, OH 43219

NEXTLINK Long Distance Services, Inc.

dba

NEXTLINK or NEXTLINK Long Distance

Regulations, Descriptions and Rates

Applicable to Furnishing

Interexchange Services

with the **State of Florida**

Douglas W. Kinkoph, Vice President
NEXTLINK Long Distance Services, Inc.
Two Easton Oval
Columbus, OH 43219

CHECK SHEET

The Title Page through Page 67 inclusive of this tariff are effective on the date shown. Original and Revised Pages as named below contain all changes from the original tariff that are in effect on the date shown.

PAGE	NUMBER OF REVISION (except as indicated)	EFFECTIVE DATE
Title	Original	
1	Original	
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3	Original	
4	Original	
5	Original	
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8	Original	
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Douglas W. Kinkoph, Vice President
NEXTLINK Long Distance Services, Inc.
Two Easton Oval
Columbus, OH 43219

TARIFF FORMAT

A. Sheet Numbering – page numbers appear in the upper right corner of the page. pages are numbered sequentially. When a new page is added between pages already in affect, a decimal is added. For example, a new page added between pages 14 and 15 would be 14.1.

B. Sheet Revision Numbers – Revision numbers also appear in the upper right corner of each page. These numbers are used to determine the most current page version on file with the **Florida Public Service Commission**. For example, the 4th revised page 14 cancels the 3rd revised page 14. Consult the Check Page for the page currently in effect.

C. Paragraph Numbering Sequence – There are nine levels of paragraph coding. Each level of coding is subservient to the next higher level:

2.
2.1
2.1.1
2.1.1.A.
2.1.1.A.1.
2.1.1.A.1. (a)
2.1.1.A.1. (a) .I.
2.1.1.A.1. (a). I. (i).
2.1.1.A.1. (a) .I. (i). (1).

D. **Check Sheets** – When a tariff filing is made with the **Florida Public Service Commission**, an updated Check Sheet accompanies the tariff filing. The Check Sheet lists the pages contained in the tariff, with a cross reference to the current revision number. When new pages are added, the Check Sheet is changed to reflect the revision. All revisions made in a given filing are designated by an asterisk (*). There will be no other symbols used on this page if these are the only changes made to it (i.e., the format, etc. remain the same, just revised revision levels on some pages.)

APPLICATION OF TARIFF

This tariff contains the regulations and rates applicable to the provision of intrastate interexchange services by NEXTLINK Long Distance Services, Inc. (hereafter the "Company") from its operating locations throughout the state of **Florida.** Service is furnished by means of wire, terrestrial microwave radio, optical, fibers, satellite circuits or a combination thereof. Service is subject to transmission, atmospheric conditions and like conditions.

Douglas W. Kinkoph, Vice President
NEXTLINK Long Distance Services, Inc.
Two Easton Oval
Columbus, OH 43219

CONCURRING CARRIERS

No Concurring Carriers

CONNECTING CARRIERS

No Connecting Carriers

OTHER PARTICIPATING CARRIERS

No Other Participating Carriers

Douglas W. Kinkoph, Vice President
NEXTLINK Long Distance Services, Inc.
Two Easton Oval
Columbus, OH 43219

EXPLANATION OF SYMBOLS, REFERENCE MARKS, AND ABBREVIATIONS OF TECHNICAL TERMS USED IN THIS TARIFF.

Revisions of this tariff are coded through the use of symbols. These symbols appear in the right margin of the sheet. The symbols and their meanings are:

(C) To signify changed conditions or regulations.

(D) To signify discontinued rate, regulation, or condition.

(I) To signify increase.

(K) To signify that material has been transferred to another sheet or place in the tariff.

(M) To signify that material has been transferred from another sheet or place in the tariff.

(N) To signify a new rate, regulation, condition, or sheet.

(O) To signify no change.

(R) To signify reduction.

(T) To signify a change in text for clarification.

Douglas W. Kinkoph, Vice President
NEXTLINK Long Distance Services, Inc.
Two Easton Oval
Columbus, OH 43219

TABLE OF CONTENTS

Douglas W. Kinkoph, Vice President
NEXTLINK Long Distance Services, Inc.
Two Easton Oval
Columbus, OH 43219

TABLE OF CONTENTS (cont'd)

1. Definitions

Access Line: An arrangement which connects the customer's location to the Company's network switching center.

Advance Payment: Part or all of a payment required before the start of service.

Authorization Code: A numerical code, one or more of which are available to a customer to enable him/her to access the carrier, and which are used by the carrier both to prevent unauthorized access to its facilities.

Authorized User: A person, firm or corporation which is authorized by the Customer or joint user to be connected to the service of the Customer or joint user.

Company: NEXTLINK Long Distance Services, Inc., the issuer of this tariff, which is a Washington corporation, or any of its affiliates which concur in this tariff.

Company Calling Card: A telephone calling card issued by the Company at the Customer's request which enables the Customer or User(s) authorized by the Customer to place telephone calls and to have the charges for such calls billed to the Customer's account.

Customer: The person, firm, or corporation which orders service and is responsible for the payment of charges and compliance with the Company's regulations.

Day: From 8:00 AM up to, but not including, 5:00 PM local time, Sunday through Friday.

Evening: From 5:00 PM up to, but not including. 11:00 PM local time, Sunday through Friday.

Holidays: The Company's recognized holidays are New Year's Day, Martin Luther King, Jr. Day, President's Day, Memorial Day, July 4th, Labor Day, Thanksgiving Day, Christmas Day.

Individual Case Basis (ICB): A service arrangement in which the regulations, rates and charges are developed based on the specific circumstances of the Customer's situation.

IntraLATA Service: Service which originates and terminates within the same Local Access and Transport Area (LATA).

InterLATA Service: Service which originates in one Local Access and Transport Area (LATA) and terminates in a different LATA.

M/M: Month to month.

Douglas W. Kinkoph, Vice President
NEXTLINK Long Distance Services, Inc.
Two Easton Oval
Columbus, OH 43219

1. Definitions (cont'd)

MOU: Minutes of use.

Night/Weekend: From 11:00 PM up to, but not including, 8:00 AM Sunday through Friday, and 8:00 AM Saturday up to, but not including, 5:00 PM Sunday.

Non-recurring Charges: The one-time initial charges for services or facilities, including but not limited to charges for construction, installation, or special fees which the Customer becomes liable at the time the Service Order is executed.

Primary InterLATA Carrier ("PIC"): Long distance carrier designated by a telephone subscriber to provide the Customer with interLATA service without having to dial a special access code..

Originating Off-net: A call originating on and placed via non-company owned facilities or a combination of non-company owned and leased facilities.

Originating On-Net: A call originating on and placed via company-owned facilities or a combination of company owned and leased facilities.

Recurring Charges: The monthly charges to the Customer for services, facilities and equipment which continue for the agreed upon duration of the service.

Service Order: The written request for communications services executed by the Customer and the Company in the format devised by the Company. The signing of a Service Order by the Customer and the acceptance by the Company initiates the respective obligations of the parties as set forth therein and pursuant to this tariff.

Station: Denotes the network control signaling unit and any other equipment provided at the Customer's premises which enables a Customer to establish communications connections and to effect communications through such connections.

Station-to-Station: Service where the person originating the call from other than a public or semi-public coin telephone dials the telephone desired and the call is completed without the assistance of a Company operator and the call is not billed to a number other than the originating number.

Two Point Message Toll Service: Furnishing of facilities for telecommunications between different local calling areas in accordance with the regulations and schedule of rates specified in this tariff.. The rates specified in this tariff are for payment for all services furnished between the calling and called stations.

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1. Definitions (cont'd)

United States: The 48 contiguous states and the District of Columbia, Hawaii, Alaska, Puerto Rico, the U.S. Virgin Islands, as well as the off-shore areas outside the boundaries of the coastal states of the 48 contiguous states to the extent that such areas appertain to and are subject to the jurisdiction and control of the United States.

User or End User: Any person or entity that obtains the Company's services provided under this tariff, regardless of whether such person or entity is so authorized by the Customer.

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2. Undertaking of the Company

2.1 Limitations on Service

2.1.1 Service is offered to the availability of facilities and the provisions of the tariff. The Company reserves the right to limit or to allocate the use of existing facilities, or of additional facilities offered by the Company, when necessary because of lack of facilities, or due to some other cause beyond the Company's control.

The furnishing of service under this tariff is subject to the availability on a continuing basis of all the necessary facilities, including facilities the Company may obtain from other carriers, to furnish service.

2.1.2 The Company reserves the right to immediately discontinue furnishing services or billing options when the manner in which the Customer uses the Company's service results, or may result, in network blockage or other service degradation which adversely affects service to the calling party, the customer, or other customers of the Company. The Company also reserves the right to immediately discontinue furnishing services or billings options, when the Customer is using the service in violation of the provisions of this tariff or in violation of the law. The customer will be responsible for all charges incurred as well as any access charges the Company may incur as a result of such customer actions.

2.1.3 Service may be discontinued by the Company, at any time and without notice to its Customers, by blocking traffic to or from certain countries, cities, NXX exchanges, or individual telephone stations, by blocking call origination for Company services, or by blocking calls using certain customer authorization codes and/or access codes when the Company deems it necessary to take such action to prevent unlawful and/or unauthorized use of its services. In addition, the Company may take any of the foregoing actions, in the case of actual or anticipated non-payment for its service. In order to control fraud, the Company may refuse to accept Calling Card, Collect Calling, and/or Third Party calls which it reasonably believes to be unauthorized or invalid and/or may limit the use of these billing options to or from certain countries or areas including, without limitation, all or part of the United States, Puerto Rico, and/or the U.S. Virgin Islands.

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2. Undertaking of the Company (cont'd)

2.1 Limitations on Service (cont'd)

2.1.4 A Customer shall not: (a) use any service mark of trade mark either of the Company or any of its affiliated companies or of which the Company or any of its affiliated companies is a licensee, or (b) refer to the Company or any of its affiliated companies in connection with any service, product, equipment offering, promotion, or publication of the customer, without the prior written consent of the Company.

2.1.5 Title to all facilities provided by the Company under these regulations remains with the Company.

2.1.6 To the extent applicable, Company service will be subject to the most recent conditions set forth in the Truth in Lending Act, Reg. Z, 12 C.F.R. Section 226.

2.1.7 If the Company disconnects a Customer's service for non-payment of past due amounts, the Customer's service will remain disconnected until such time as the Company receives payment for all past due amounts and confirms the availability of sufficient funds to satisfy the amount of payment.

2.1.8 The Company assumes no responsibility for the availability or performance of any cable or satellite systems or related facilities under the control of other entities, or for other facilities provided by other entities used for service to the Customer, even if the Company has acted as the Customer's agent in arranging for such facilities or services. Such facilities are provided subject to such degree of protection or non-preemptability as may be provided by the other entities.

2.1.9 The Company makes no warranties or representations, express or implied either in fact or by operation of law, statutory, or otherwise, including warranties of merchantability or fitness for a particular use, except those expressly set forth herein.

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3. Rules and Regulations

3.1 Terms and Conditions

3.1.1 Company services are provided and billed on the basis of a minimum period of at least one month, beginning on the date that billing becomes effective and continues to be provided until canceled by the Customer in writing on not less than 30 days notice from the date of postmark on the letter giving notice of cancellation.

3.1.2 The name(s), address(es), and telephone number(s) of the Customers desiring to use the service must be stipulated in the application for service.

3.1.3 The Customer agrees to operate the Company-provided equipment in accordance with the instructions of the Company or an agent of the Company.

3.1.4 The Customer agrees within five (5) days of termination of the service in connection with which the equipment was used to return to the Company all Company-provided equipment delivered which was delivered to the Customer. Said equipment shall be in the same condition as when delivered to the Customer, normal wear and tear excepted. Customers shall reimburse the Company, upon demand, for any costs incurred by the Company due to the Customers failure to comply with this provision.

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3. Rules and Regulations (cont'd)

3.2 Liability

3.2.1 Except for granting allowances for interruptions of service as provided for in Section 3.22 and other sections of this tariff, the Company shall not be liable for any failure of performance due to: causes beyond its control, including, but not limited to, acts of God, fires, floods or other catastrophe, national emergencies, insurrections, riots or wars, strikes, lockouts, work stoppages or other labor difficulties; other preemption of existing services to restore service in compliance with Part 64, Subpart D, Appendix A, of the FCC's Rules and Regulations; or any law, order, or action of any governing authority or agency thereof.

3.2.2 The Company's liability, if any, with regard to the delayed installation of Company facilities or commencement of services shall not be liable to a Customer or third party for any direct, indirect, special, incidental, reliance, consequential, exemplary, or punitive damages, including, but not limited to, loss of revenue or profits, for any reason whatsoever, including, but not limited to, any act or omission, failure to perform ordering (including the reservation of any specific number for use with a service), installation (including delays thereof), offered under this tariff, and subject to the provisions of Section 3.2, following the Company's liability, if any shall be limited as follows:

(1) With respect to any Dedicated leased Line Service offered by the Company, the Company's liability amount is equal to the proportionate monthly recurring charge or charges for the service for the period during which the service was affected.

(2) With respect to any service provided by the Company which involves dedicated access, shared interexchange transmission, and/or shared information, the Company's liability shall not exceed an amount equal to the proportionate monthly recurring charges—including any service charges, minimum monthly charges, basic feature package charges monthly charges for optional features, charges for dedicated access facilities and any other monthly charges—for the period during which the service was affected or, if only a transmission using the shared interexchange facilities is interrupted, an amount equal to the charge applicable to a one-minute call to the called station at the time the affected call was made. Where any claim arises out of

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3. Rules and Regulations (cont'd)

3.2 Liability (cont'd)

3.2.2 (cont'd)

(2) (cont'd)
the Company's acting as a Resp Org, or performing SMS Res Org changes, or where any claim arises out of any and all failing by the Company in connection with the provision of 800/888/877 (and future toll-free prefixes) service is not made available on the date committed to the customer, or cannot otherwise be made available after the Company's acceptance of the Customer order, or is provided with a number or numbers other than the one(s) committed by the Company to the Customer, or the number or numbers are not included in 800/888/877 Service Directory Assistance or are included in an incorrect form, and any such failure or failures is due solely to the negligence of the Company, in such cases the Company's liability, if any, will be limited to the lessor of: (a) the actual monetary damages incurred and proven by the Customer as the direct result of such failure to failures; or (b) the sum of $1000.00. With respect to Resp Org and SMS Resp Org Changes, the customer will indemnify and hold the Company harmless against any third party claims arising out of the execution of changes requested by the Customer, including those changes made by an 800/888/877 Subscriber. Where the Resp Org Service Customer is a Customer acting on behalf of an 800/888/877 Subscriber, the Customer represents that it has the authority to act on the 800/888/877 Subscribers behalf in choosing a Resp Org and otherwise utilizing the Company's Resp Org Service. The Company shall not be liable at all for the use, misuse, or abuse of a Customer's 800/888/877 Service by third parties including, without limitation, the Customers' employees or members of the public who dial the Customers 800/888/877 number by mistake. Compensation for any injury the Customer may suffer due to the fault of people or entities other than the Company must be sought from other such parties.

3. Rules and Regulations (cont'd)

3.2 Liability (cont'd)

3.2.2 (cont'd)

(3) With respect to any service provided by the Company which involves shared access, shared interexchange transmission, and/or shared termination. The Company's liability shall not exceed an amount equal to the charge applicable to a one(1) minute call to the called station at the time the affect call was made.

(4) With respect to any service provided by the Company's which involves dedicated access, shared interexchange transmission, and/or dedicated termination, the Company's liability shall not exceed an amount equal to the charge applicable to a one (1) minute call to the called station at the time the affected call was made.

(5) With respect to the routing of calls by the Company to public safety answering points or municipal emergency service providers, the Company's liability, if any, will be limited to the lessor of: a) the actual monetary damages incurred and proved by the customer as the direct result of the Company's action, or failure to act, in routing the call; or b) the sum of $1000.00.

(6) With respect to the Company's offering of Telecommunications Relay Service (TRS), any service provided by LCI which involves receiving, translating, or delivering messages by telephone, text telephone, a Telecommunications Device for the Deaf, or any other instrument over the facilities of the Company or any connecting carriers or through any TRS centers operated by the Company or its agents, the Company's liability shall not exceed an amount equal to the Company's charge for a one (1) minute call to the station at the time affected call was made.

The liability provided for above, shall in each case, be in addition to any amounts that may otherwise be due to the Customer under this tariff as a credit allowance for the interruption of service.

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3. Rules and Regulations (cont'd)

3.2 Liability (cont'd)

3.2.3 The Company shall be indemnified, defended, and held harmless by the Customer or by others authorized to use the service against all claims of loss or damage arising from the use of service furnished under this tariff, including:

(a) Claims for libel, slander, invasion of privacy, or infringement of copyright arising out of the material, data, information, or other content transmitted via Company service;

(b) patent infringement claims arising from combining or connecting Company service with apparatus and systems furnished by the Customer or others; and

(c) all other claims arising out of any act or omission of the Customer or others including those relating to Section 3.2.4 below, in connection with any service provided by the Company.

3.2.4 The Company shall not be liable for any act or omission of any other company or companies furnishing a portion of the service, or for damages associated with service, circuits, or equipment that it does not furnish, or for damages which result from the operation of customer-provided systems, equipment, facilities or services which are interconnected with Company services.

3.2.5 The Company does not guarantee, nor make any warranty with respect to, service installations at locations at which there is present an atmosphere that is explosive, prone to fire, dangerous or otherwise unsuitable for such installations. The Customer and user shall indemnify and hold the Company harmless from any and all loss, claims, demands, suits or other actions, or any liability whatsoever, whether suffered, made instituted or asserted by the Customer by any other party, for any personal injury to, whether owned by the Customer or others, caused or claimed to have been caused, directly or indirectly, by the installation, operation, failure to operate, maintenance, removal, presence, furnished by the Company at such locations.

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3. Rules and Regulations (cont'd)

3.2 Liability (cont'd)

3.2.6 The Company is not liable for any defacement of, or damages to, the premises of a Customer resulting from the furnishing of service, or the attachment of any instruments, apparatus associated wiring on such Customer premises or from the installation or removal thereof, when such defacement or damage is not the result of Company negligence.

3.2.7 The Company shall not be liable for the Customers failure to fulfill its obligations to take all necessary steps including, without limitation, obtaining, installing and maintaining all necessary equipment, materials, and supplies, for interconnecting the terminal equipment or communications system of the Customer, or any third party acting as its agent, to the Company's network. The Customer shall secure all licenses, permits, approvals, rights-of-way, and other arrangements necessary for such interconnection. In addition, the Customer shall ensure that its equipment and/or system or that of its agent is properly interfaced with the Company's service, that the signals emitted into the Company's network are of the proper mode, bandwidth, power, data speed, and signal level for the intended use of the Customer and in compliance with the criteria set forth in the following, and that such do not damage the Company's equipment or network or injure Company personnel or degrade service to other Customers. If the Federal Communications Commission or some other appropriate certifying body certifies terminal equipment as being technically acceptable for direct electrical connection with interstate communications service, the Company will permit such equipment to be connected with its services without the use of protective interfaces devices. If the Customer or its agent fails to maintain and operate its equipment and/or system or that of its agent properly, with resulting imminent harm to Company equipment, network, personnel, or the quality of service to other Customers, the Company may, upon notice, require the use of protective equipment at the Customers expense. If this fails to produce satisfactory quality and safety, the Company may, upon written notice, terminate the Customers service without liability or obligation.

3.2.8 With respect to the Company's prepaid Calling Card Service, the Company makes no warranty, guarantee, or representation, either express or implied, regarding the merchantability, accuracy, reliability, condition, or fitness of the information provided in connection with the use of the card.

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3. Rules and Regulations (cont'd)

3.2 Liability (cont'd)

3.2.9 Use and Sale of Telephone Subscriber Information

3.2.9.1 With respect to the use and sale of telephone subscriber information provided pursuant to Automatic Number Identification ("ANI") or charge number services, the Company shall permit the Customer to use the telephone number and billing information or billing and collection, routing, screening and completion of the originating telephone subscriber's call or transaction, or for services directly related to the originating telephone subscriber's call or transaction. The Customer is prohibited from reusing or selling the telephone number or billing information without first:

(a) notifying the originating telephone subscriber and:

(b) obtaining the affirmative consent of each subscriber for such reuse or resale. Additionally, the Customer is prohibited from disclosing, except as permitted above, any information derived from the Automatic Number Identification ("ANI") or charge number service for any purpose other than:

(i) performing the services or transactions that are the subject of the origination telephone subscriber's call;

(ii) ensuring network performance security, and the effectiveness of call delivery;

(iii) compiling, using, and disclosing aggregate information; and

(iv) complying with applicable law or legal process.

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3. Rules and Regulations (cont'd)

3.2 Liability (cont'd)

3.2.9 Use and Sale of Telephone Subscriber Information (cont'd)

3.2.9.2 The requirements imposed under Section 3.2.9.1 shall not prevent a person to whom automatic number identification, or charge number services are provided from using:

(i) the telephone number and billing information provided pursuant to this service; and

(ii) any information derived from the automatic number identification or charge number service, or from the analysis of the characteristics of a telecommunications transmission, to offer a product or service that is directly related to the products or services previously acquired by that Customer from such person.

3.3 Cancellation of Service by a Customer

3.3.1 If a Customer cancels an order for service before the service begins, before completion of the minimum period, or before completion of some other period mutually agreed upon by the Customer and the Company, a charge will be levied upon the Customer for the non-recoverable portions of expenditures or liabilities incurred expressly on behalf of the Customer by the Company and not fully reimbursed by installation and monthly charges. If based on an order by a Customer, and construction has either begun or been completed, but no services provided, the non-recoverable cost of such construction shall be borne by the Customer.

3.3.2 Except as otherwise provided in this tariff, if an order for installation is delayed for more that thirty (30) days beyond the due date, and such delay is not requested or caused by the Customer, the Customer may cancel the order without incurring cancellation charges.

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3. Rules and Regulations (cont'd)

3.4 Use of Service

3.4.1 Service furnished by the Company may be used for one or more of the following:

(a) for the transmission of communications by the Customer;

(b) for the transmission of communications to or from an authorized user or joint user;

(c) for the transmission of communications to or from a Customer of another common carrier, which has subscribed to the Company's communications service for purposes of resale.

3.4.2 Service furnished by the Company may be arranged for joint use or authorized use. The joint user or authorized user shall be permitted to use such service in the same manner as the Customer, but subject to the following:

(a) One joint user or authorized user must be designated as the Customer. The designated Customer does not necessarily have to have communications requirements of its own. The Customer must specifically name all joint users or authorized users in the application for service. Orders that involve the start, rearrangement, or discontinuance of joint use or authorized use service will be accepted by the Company only from that Customer and will be subject to all provisions of this tariff.

(b) All charges for the service will be computed as if the service were to be billed to one Customer. The joint user or authorized user that has been designated as the Customer will be billed for all components of the service and will be responsible for all payments to the Company. In the event that the designated

3. Rules and Regulations (cont'd)

3.4 Use of Service (cont'd)

3.4.2 (b) (cont'd)

Customer fails to pay the Company each joint user or authorized user shall be liable to the Company for all charges incurred as a result of its use of the Company's service. Each joint or authorized user must submit to the designated Customer a letter accepting contingent liability for its portion of all charges billed by the Company to the designated Customer. This letter must specify that the joint or authorized user understands that the Company will receive a copy of the guaranty from the designated Customer. Unless supportive services are provided, the Customer shall be responsible for allocating charges to each joint user or authorized user.

3.5 Directory Assistance

3.5.1 Directory Assistance is available for all services. The Directory Assistance charge will be applied to each call for information as to any telephone number in the United States, Puerto Rico, and the U.S. Virgin Islands. The Directory Assistance charge applies to each call regardless of whether the requested Directory Assistance telephone number is furnished. In addition, Directory Assistance calls will not count toward, nor be calculated as part of, the Customers service volume discounts unless otherwise indicated. Directory Assistance customer calls may be placed with the assistance of an operator, and they may be billed to commercial credit cards.

3.5.2 A credit allowance will be given or the charge that would otherwise apply will be waived when:

(a) the Customer experiences poor transmission or is cut-off during the call to Directory Assistance;

(b) the Customer is given an incorrect telephone number by the Directory Assistance operator;

(c) the Customer has inadvertently misdialed and has reached Directory Assistance for the wrong area code. To obtain such a credit/waiver, the Customer must notify a Company customer service representative with twenty-four (24) hours.

3. Rules and Regulations (cont'd)

3.5 Directory Assistance (cont'd)

3.5.3 Customers who are presubscribed to Company service and have been certified in writing to be unable to access or use a manual directory because of a visual or other physical impairment are eligible to receive a credit that will be applied against the per-call charge and any applicable operator-assistance surcharges specified in this tariff for domestic Directory Assistance calls made by dialing area code +555+1212. This certification must be made by a licensed physician, optometrist, appropriate federal or state agency, or appropriate approved private agency.

The written certification of visual or other physical impairment must be provided to a Company Customer Service Representative, or at the Company's election, proof of certification, as defined above, may be provided to, and maintained on file with, the Customer's Local Exchange Carrier.

Credits may be used by: (I) the visually or otherwise physically impaired customer: (ii) an organization established specifically for the purpose of assisting the visually or otherwise physically impaired; or (iii) a business where all owner(s) and/or employees of the business on the premises at which a call originates have been certified as visually or otherwise physically impaired. Credits will apply only to Directory Assistance calls made by dialing area code+555+1212, that originate from and are billed to the telephone number of the certified visually or otherwise physically impaired person or organization. Only one telephone number per location is entitled to this credit. A maximum of fifty (50) Directory Assistance calls, including operator-assistance surcharges, per monthly billing period will be eligible for the credit.

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3. Rules and Regulations (cont'd)

3.6 Toll Free Service

3.6.1 A call begins when call termination is received by or passes through customer premises equipment. It is the Customer's responsibility to pass appropriate answer supervision back to the Company point of connection.

3.6.2 If a Customer of the Company Toll Free service is found to be non-compliant in passing back appropriate answer supervision. The Company reserves the right to suspend and/or deny service. The Company shall give the Customer three (3) days notice of intent to suspend or deny service due to such non-compliance.

3.6.3 The Customer shall be liable for all costs and toll charges associated with their 800/888/877 service, including unauthorized calls associated with the use of 800/888/877 service obtained from the Company, including, but not limited to, calls made using Toll Free Service when such calls are in any way routed through the Customer's location. Customers shall maintain sole responsibility for the security of 800/888/877 number(s) issued to them.

3.6.4 Nothing in this section, or, in any other provision of this tariff, or in any marketing materials issued by the Company, shall give any Customers who have reserved 800/888/877 telephone numbers hereunder or Customer who subscribe to and use Toll Free Service, or their transferees or assignees, any ownership interest or proprietary right in any particular 800/888/877 telephone number.

3.6.5 Customers (including carrier customers) are prohibited from using any telephone numbers beginning with an 800/888/8/77 service code, or any other number advertised or widely understood to be Toll Free, in a manner that would result in; (a) the calling party or the subscriber originating line being assessed any fee or charge by virtue of completing the call; (b) the calling party being connected to a pay-per-call service; (c) the calling party being charges for information conveyed during the call unless the calling party has a presubscription or comparable arrangement; or (d) the calling party being call back collect for the provision of audio or data information services, simultaneous voice conversation services, or products. The Customer shall be afforded a period of no less that seven (7) days and no more than fourteen (14) days during which a violation may be brought into compliance. 800/888/877 service no in compliance with the above regulations at the expiration of such period may be terminated immediately.

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3. Rules and Regulations (cont'd)

3.6 Toll Free Service (cont'd)

3.6.6 The Customer must obtain an adequate number of access lines associated with Toll Free service(s) to handle the Customer's expected demand in order to prevent interference or impairment of this service, or any other service provided by the Company, taking into account (1) call volume (2) average call duration; (3) time-of-day characteristics; and (4) peak calling periods. The Company, without incurring any liability, may disconnect or refuse to furnish Toll Free services to any Customer that fails to comply with these conditions. Incase of disconnection, the Customer will be notified at least (5) days in advance of the disconnect. The Customer will be responsible for all charges incurred as well as any access charges the Company may incur as a result of the Customer failure to comply within the above conditions.

3.6.7 A Customer is responsible for all charges for network arising from calls placed to the Customer's Toll Free service. An applicant for Toll Free service may be required to supply the following information when requesting service: an initial traffic forecast, identification of its geographical marketing target areas, and a schedule of marketing and promotional activities. A new tariff forecast shall be submitted quarterly after service is initiated. Customers of Toll Free service may not use Automatic Number Identification (ANI), provided by the Company incidental to the furnishing of Toll Free service, to invoice, either directly or indirectly their Customer in connection with their furnishing of other than common carrier services.

3.6.8 All new 800/888/877 and future toll free prefixes, for the purpose of this tariff, apply to all Company existing 800/888/877 services, rates, and rules and regulations that governs all Company Toll Free service.

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3. Rules and Regulations (cont'd)

3.6 Toll Free Service (cont'd)

3.6.9 Reservation and Administration, Ownership, Use, and Assignment of Telephone Numbers for NEXTLINK 800

3.6.9.1 The Company will accept a prospective Customer's request for a particular 800/888/877 service telephone number. Up to a total of ten (10) such requested numbers may be requested. The Company will accommodate each request to the possible extent. If a requested number(s) can be assigned to a prospective Customer, the Company will notify the Customer and will reserve it for the Customer's use for a fifty-nine (59) day period. If, at the end of the fifty-nine (59) day period, the prospective Customer has not subscribed to the Company 800/888/877 services using a reserved number(s), the Company, in accordance with its procedures, may make the reserved number available for use by another Customer.

3.6.9.2 In its capacity as Resp Org, the Company will reserve, assign, activate, or change, upon receipt of a verified request, 800/888/877 numbers for a Customer or prospective Customer and will administrator 800/888/877 numbers, in accordance with customary industry standards and practices, the terms of this tariff, and the effective procedures of the 800/888/877 Service Management System (SMS) database administration. Customers may request, reserve, assign or activate 800/888/877 numbers on their own behalf, or a Customer that resells Company inbound transmission services may request, reserve, assign, or activate 800/888/877 numbers on behalf of a Customer or prospective Customer of such reseller. A Customer who resells Company inbound transmission services must provide to any Customer or potential Customer, upon reasonable request therefore, information concerning the status of a particular 800/888/877 number or number(s) in which the Customer or potential Customer has interest and, if applicable and available the identity of the Resp Org(s) for the 800/888/877 number(s), the Customer must notify the Company within forth-eight (48) hours so the Company may release the 800/888/877 numbers to the pool of numbers for assignment in accordance with industry practice and standards.

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3. Rules and Regulations (cont'd)

3.6 Toll Free Service (cont'd)

3.6.9 Reservation and Administration, Ownership, Use, and Assignment of Telephone Numbers for NEXTLINK 800 (cont'd)

3.6.9.3 800/888/877 numbers are incidental to the inbound calling service with which they are associated and, as such, may not be sold, transferred, or otherwise conveyed independent of inbound transmission. The assignment of an 800/888/877 telephone number(s) for use with company-provided inbound transmission service confers of the Customer no proprietary interest what so ever in the number(s) assigned. It shall be a violation of this tariff if the Customer seeks to acquire, or does acquire, any 800/888/877 associated with inbound service provided by the Company for the primary purpose of selling, brokering bartering, or releasing for a fee (or other consideration) to another party that 800/888/877 number, independent of the Company service with which it is associated. In any instance in which the Company learns that a Customer or prospective Customer is attempting to sell or otherwise transfer or assign an 800/888/877 number to another person, in violation of this tariff, the Company may immediately and without notice release the number from reserved status, or it may immediately upon written notice to the Customer discontinue the furnishing of service, or it may immediately upon written notice to the Customer discontinue the furnishing of service via the 800/888/877 number. The Company telephone number forfeited as a result of the impermissible or reassigned to the undertaking will not be reserved for the prospective Customer or reassigned to the Customer under any condition or circumstances by the Company.

3.6.9.4 Each 800/888/877 service telephone number must be placed in actual and substantial use by the Customer.

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3. Rules and Regulations (cont'd)

3.7 Recording Conversations

3.7.1 Company services are not adapted to the use of recording devices to record two-way telephone conversations, or for other purposes, do so at their own risk. As used in this section, a two-way conversation is a telephone conversation between or among two or more parties. A Customer may use a recording only if the Customer is able to connect or disconnect the recording, or turn the recording device on or off, at will.

3.7.2 A Customer may record a two-way conversation only when the recording is:

(a) preceded by verbal or written consent of all parties to the conversation;

(b) preceded by verbal notification of the recording of the conversation, which notification is recorded at the beginning, and as a part of, the call; or

(c) accompanied by a distinctive recorder tone, repeated at intervals of approximately fifteen (15) seconds, to alert all parties to the conversation that a recording device is in use.

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3. Rules and Regulations (cont'd)

3.7 Recording Conversations (cont'd)

3.7.3 Broadcast licenses are exempt from the restrictions set forth in Section 3.7 when the licensee is recording the two-way conversation for broadcast and:

(a) the licensee informs each party to the conversation that the licensee intends to broadcast the conversation;

(b) each party to the conversation is aware that the conversation will be broadcast; or

(c) the other party or parties to the conversation may be presumed to be aware, from the circumstances of the conversation, that the conversation is likely to be broadcast; provided that such awareness may be presumed only when the other party to the conversation is associated with the licensee (such as an employee or part-time reporter) or the other party or parties to the conversation originate(s) and the conversation is obviously in connection with a program during which the licensee customarily broadcasts telephone conversations.

3.7.4 A Customer is exempt from the restrictions set forth in Section 3.7 when:

(a) recording incoming calls made to telephone numbers publicized for emergencies (such as 911) and outgoing calls made in immediate response to these incoming calls (including calls made to and from Department of Defense Command Centers and the Operations Center of the Nuclear Regulatory Commission);

(b) recording calls made for patently unlawful purposes (such a bomb threats, kidnap ransom requests, and obscene calls) and outgoing calls made in immediate response to these calls (including calls referred to the U.S. Secret Service that threaten the safety and security of the President of the United States, his or her immediate family, or the White House); or

(c) recording calls pursuant to an explicit and lawful order of a court issued to 18 U.S.C. Section 2516, as amended, or any equivalent successor provision.

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3. Rules and Regulations (cont'd)

3.8 Operator Services

3.8.1 A Customer acquiring operator service from the Company which, in the ordinary course of its operations, makes telephone calls, must:

(a) post on or near the telephone instrument, in plain view of consumers: the name address and toll-free telephone number of the provider of operator services;

(b) a written disclosure that the rates for all operator-assisted calls are available on request, and that consumers have a right to obtain access to the interstate common carrier of their choice; and that Customers may contact their preferred interstate common carriers for information on accessing that carrier service using the telephone; and the name and address of the enforcement of the Common Carrier Bureau of the Federal Communications Commission, to which the consumer may direct complaints regarding operator services; ensure that each of its telephones presubscribed to a provider of operator services allows consumers to use 800/888/877 and 950 access code numbers or any other carrier identification code (1010XXX) to obtain access to the provider of operator service desired by the consumer;

(c) ensure that no charge by such Customer to the consumer for using an 800/888/877 and 950 access code, or any other access code number, is greater than the amount the aggregator charges for calls placed using the Customers presubscribed provided of operator services. Payment (on a location-by-location basis) of any compensation to the Customer, including commissions, shall be in violation of Section 3.8.1 (b) and shall not be made until such time as the blocking ceases.

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3. Rules and Regulations (cont'd)

3.9 Information Provider Data

A Service Bureau shall promptly furnish to the Company, and keep current on a continuing basis, the name, address, and Customer Service telephone number(s) of the Information Providers to whom it provides service. Where an Information Provider directly subscribes top Company service, it shall promptly furnish to the Company, and keep current on a continuing basis, its name, address, and Customer Service Telephone number(s).

3.10 Line Service

No provider of pay-per-call services subscribing to the Company's service in this tariff shall use automatic dialing devices which deliver a recorded message to the called party unless the device releases that called party's telephone line promptly but in no event longer than current industry standards.

3.11 Answer Supervision

Answer supervision must be provided when a Company service offering is connected to switching equipment or a Customer-provided communications system. The Customers equipment or system must provide answer supervision so that the measure of chargeable time that begins upon the delivery of the Customer's call to the switching equipment or to the equipment connected to the communications system and ends upon termination of the call by the calling party. If a Customer's communications system fails to promptly return to Company am idle (on-hook) state upon completion of the call, the Customer will be held responsible for all charges that responsible for all charges that result up until the time the Customer's communication system signals the Company's network that the call has been terminated or until such a time that the Company's own system terminates the call.

3. Rules and Regulations (cont'd)

3.12 Restrictions

Providers of pay-per-call services subscribing to Company transmission services, including 900 service, must comply with all requirements of (a) Title I and II of the Telephone Disclosure and Dispute Resolution Act (Pub.L No. 102-556) (TDDRA); and (b) all requirements of: the regulations presubscribed by the federal Communications Commission and Federal Trade Commission pursuant to those Titles. The Company shall terminate programs which utilize 900 service if the programs are not in compliance, following written notice to the provider. The provider shall be afforded a period of no less than seven (7) days and no more that fourteen (14) days during which a program may be brought into compliance. Programs not in compliance at the expiration of such period shall be terminated immediately.

3.13 Payment Arrangements

3.13.1 The Customer is responsible for payment of all charges for service furnished to the Customer or its joint or authorized users. This responsibility is not changed by virtue of any use, misuse, or abuse of the Customer service or Customer provided systems, equipment, facilities, or services interconnected to the Customer's service, which use, misuse, or abuse may be occasioned by third parties, including, without limitation, the Customers' employees or other members of the public. The Company is not liable for any damages, including toll usage charges, the subscriber may incur as a result of the unauthorized use of its telephone facilities. This unauthorized use if the subscriber's facilities includes, but is not limited to, the placement of calls from the subscriber's premises, and the placement of calls through subscriber-provided equipment which are transmitted or carriers on the Company network. The Company security department may work with subscribers to recommend possible solutions to reduce unauthorized use of its facilities. However, the Company does not warrant or guarantee that its recommendations will prevent all unauthorized use, and the subscriber is

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3. Rules and Regulations (cont'd)

3.13 Payment Arrangements (con't)

3.13.1 (cont'd)
responsible for controlling access to, and use of, its own telephone facilities. Non-recurring charges are payable when the service for which they are applied has been made available. If an entity other than the Company (e.g. another carrier or supplier) imposes charges on the Company, in addition to its own internal costs, those charges will be passed onto the Customer. Recurring charges which are fixed in amount and not dependent on usage are billed in advance. Except for usage charges the rate or volume discount level applicable to a Customer for a particular service or services shall be the rate or volume discount level in effect at the end of the monthly billing period applicable to the Customer for the particular service or service. The Customer agrees to pay the Carrier for all charges billed as a result of any use of the Customer's authorization code(s), whether such use is by Customer or by a third party in connection with a lost, stolen or misappropriated authorization code, or otherwise. It is the Customer's responsibility to inform the Company that an authorization code(s) has been stolen or lost.

3.13.2 Service is provided and billed on a monthly(30-day) basis, beginning on the date that service becomes effective.

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3. Rules and Regulations (cont'd)

3.13 Payment Arrangements (cont'd)

3.13.3 Payment will be due upon receipt. Interest may be applied in accordance with Company-standard credit policy to any unpaid amount commencing thirty (30) days after the statement date.

3.13.4 If a Customer accumulates more that $500.00 of unpaid or disputed Toll Free service charges, the Company Resp Org reserves the right not to honor that Customer's request for a Resp Org change until such dispute is resolved or undisputed charges are paid in full.

3.13.5 In the event the Company incurs fees or expenses, including attorney's fees in collecting or attempting to collect any charges owed the Company, the Customer will be liable to the Company for the payment of all such fees and expenses reasonably incurred.

3.13.6 The Company's bills are payable upon receipt, unless the Company indicates on the invoice or a billing insert that the sum shown as due need not be paid, because of the smallness of the amount, until the balance reaches some specified amount; or the Company may deal with Customers whose accounts show very small balances by withholding the issuance of an invoice until the amount due from the Customer reaches a level, which, in the Company's sole discretion, is deemed large enough to justify initiating the billing and collection process; or the Company may invoice low usage Customers every other month unless a Customer invoiced in such a manner requests monthly billing. When a bill is issued, amounts not paid within thirty (30) days after the date of invoice will be considered past due. If the Company becomes concerned at any time about the ability of a Customer to pay its bills, the Company, in its sole discretion, may require that such a Customer pay its bills within a specified number of days and to make such payments in cash or the equivalent of cash.

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3. Rules and Regulations (cont'd)

3.13 Payment Arrangements (cont'd)

3.13.7 Applicants for service or existing Customers whose financial condition is not acceptable to the Company, or is not a matter of general knowledge, may be required at any time to provide the Company a security deposit as a condition of service. The deposit requested will be in cash or the equivalent of cash, up to an amount equal to the applicable installation charges, if any, and/or up to one month's actual or estimated usage charges for service to be provided. Any applicant or Customer may also be required, at any time, whether before or after the commencement of service, to provide such other assurances of, or security for, the payment of the Company's charges for services to be provided as the Company deems necessary including, without limitation, advance payments for service, third party guarantees of payment, pledges, or other grants of security interest in the Customers' assets, and similar arrangements. The required deposit or other security may be increased or decreased by the Company as it deems appropriate in light of changing conditions and Customers usage pattern. In addition, the Company shall be entitled to require such an applicant or Customer to pay all its bills within a specified period of time, and to make such payments in cash or the equivalent of cash. Simple interest at the rate of six percent (6%) annually will be paid for the period during which the deposit is held by the Company, unless a different rate has been established by the appropriate legal authority in the jurisdiction in which the Company service in question is provided. At the Company's option, such deposit may be refunded to the Customer's account at any time. The Company also reserves the right to cease accepting and processing service orders after it has requested a security deposit and prior to the Customer's compliance with this request.

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3. Rules and Regulations (cont'd)

3.13 Payment Arrangements (cont'd)

3.13.8 For the purpose of billing, the start of service date is the activation date. The end of service date is the last day of the minimum notification period as described in Section 3.1.1.

3.13.9 If a Customer does not give the Company written notice of a dispute within sixty (60) days from the date the invoice was rendered, such invoice shall be deemed to be correct and binding on the Customer.

3.13.10 The charges set forth in this tariff contemplate installations made in normal locations and under normal working conditions. Any installations to be made under other circumstances are subject to additional charges.

3.13.11 Promotional and other credits offered by the Company in the marketing of its service cannot be assigned, but must be used by the person to whom they were offered and who earned them in strict accordance with the terms of the offers. In the event that a customer has been awarded a promotional credit for subscribing to the Company and does not use the service within twelve (12) months following the date of the Customer's service order, the Company may cancel the credit from the Customer's account unless otherwise stated in the specific promotion.

3.13.12 All charges for service are exclusive of applicable federal, state, local taxes, and tax-related surcharges.

3. Rules and Regulations (cont'd)

3.13 Payment Arrangements (cont'd)

3.13.13 If a Customer whose account has been closed has a credit balance showing, the Company will transfer the credit to another account of the Customer, if there is one, or will mail a check for the balance to the Customer if it believes it has a valid and current address. If the Company is not certain that it has a valid and current address, it will include a notice with the final invoice, which will be mailed to the Customer's last known address, asking the Customer to verify the address so that it can make a refund, or it will write to the Customer at that address and request verification. Such verification can be made by calling a designated telephone number or by writing to a specified address. Upon receiving verification, a check for the balance will be mailed. If the final invoice or the notification letter is returned by the post office as undeliverable, or if no response is received within thirty (30) days of mailing, the Company as its option may begin applying a closed account maintenance charge of $2.50 per month in the second monthly billing period following the month in which the account was closed, and will continue to apply that charge until the Customer requests a refund in writing or the balance is exhausted.

3.13.14 From time to time, the Company will grant credits against usage or recurring charges in an amount not to exceed $1000.00 per Customer or account, per monthly billing period, whenever the Company determine, in its sole discretion, that such a credit is warranted due to consideration or disputes involving the delivery of past service to the Customer or account receiving the credit.

3.13.15 In lieu of the Customer receiving applicable volume discounts and/or promotional credits on a monthly invoice, the Company may, in its sole discretion, utilize other forms of payment.

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3. Rules and Regulations (cont'd)

3.13 Payment Arrangements (cont'd)

3.13.16 In the event payment is made by check and the Customer's check is not honored by the institution on which it was drawn, the Company will impose, and the Customer will be required to pay, a $15.00 fee, in addition to other tariff, legal, and equitable remedies available to the Company.

3.13.17 If the Company disconnects a Customer's service for non-payment of past due amounts, the Customer's service will remain disconnected until such time as the Company receive payment for all past due amounts and confirms the availability of sufficient funds to satisfy the amount of payment.

3.13.18 The liability of the Company for errors in billing that result in overpayment by the Customer shall be limited to a credit equal to the dollar amount erroneously billed.

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3. Rules and Regulations (cont'd)

3.13 Payment Arrangements (cont'd)

3.13.19 A surcharge will be imposed on all Customer's charges for outbound service originating at, or inbound service terminating at, addresses in states which levy, or assert a claim of right to levy: a) gross receipts tax on the Company's operations in any such state; or b) a tax on interstate access charges incurred by the Company for access to telephone exchanges in that state; or c) an ad valorem tax on the Company's interstate property located in that state. This surcharge is based, respectively, on the Company's: a)gross receipts or revenues in that state; and/or, b) payment of interstate access charges in that state; and/or, c) property located in that state and used by the Company to provide interstate service. The surcharge for (c) is derived by using the ratio of interstate revenue in that state to total revenue, multiplied by total ad valorem taxes imposed during the current calendar year and are listed below. The surcharge will be shown as a separate line item on the Customer's invoice.

STATE	SURCHARGE	
FL	0.9780%	(N)

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3. Rules and Regulations (cont'd)

3.14 Special Access Surcharge (cont'd)

3.14.1 A monthly special access surcharge, required by the Local Exchange Carrier (LEC), applies to each local channel termination associated with Channel Service and Foreign Exchange Service Capability. This monthly surcharge is applicable when the local channel is connected to a PBX or equivalent device which is capable of interconnecting the Channel Service or Foreign Exchange Service Capability with local exchange service. When analog or digital high capacity facilities interconnect with the local exchange network, the special access surcharge is applied on a per voice grade equivalent circuit basis as shown in the following example:

Basic Digital Facility Circuits		Voice Grade Equivalent $25		Monthly Surcharge Per Circuit
	X			
Group		12 X $25	=	$300.00
DS1		24 X $25	=	$600.00

3.14.2 The special access surcharge applies on each local channel termination installed whether the interconnection capability exists in the Customer's premise equipment or in a Centrex CO type switch.

3.14.3 The Customer may be exempt from the monthly special access surcharge if:

(a) The Customer certifies in writing that the local channel terminated is a device not capable of interconnecting the service with the local exchange network; or

(b) The Customer certifies that the local channel termination, by nature of its operating characteristics, could not make use of LEC common lines; or

(c) The Customer certifies that the local channel is connected to a LECs switched access service that is subject to carrier line charges.

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3. Rules and Regulations (cont'd)

3.14 Special Access Surcharge

3.14.4 The certification will be in the form of a written notification to the Company. The notification may be provided:

(a) At the time the service is ordered;

(b) At such time as the service is re-terminated to a device not capable of interconnecting to the local exchange network; or

(c) At such time as the local channel becomes associated with a switched access service that is subject to carrier common line charges.

3.14.5 If a written certification is not received at the time an order for new service is placed, the special access surcharge will be applied. The Company will cease billing the special access surcharge and the exempt status will become effective on the date the certification is received by the Company on services in place. If the Company charged the Customer prior to the receipt of the exemption certification, the Company will credit the Customer's account, not to exceed ninety (90) days, based on the effective date of the change specified by the Customer in the letter of certification.

3.15 Gross Receipts and Other Taxes

A surcharge will be imposed on all charges for outbound service originating at, or inbound service terminating at, addresses in states which levy, or assert as claim if right to levy, a gross receipts tax on the Company's operations in any such state, or a tax on interstate access charges incurred by the Company for originating access to telephone exchanges in that state. This surcharge is based on the particular state's receipts tax and other states receipts taxes imposed directly or indirectly upon the Company by virtue of and measured by the gross receipts or revenues in that state and/or payment of interstate access charges in that state. The surcharges will be shown as a separate line item on the Customer's notice.

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3. Rules and Regulations (cont'd)

3.16 Telecommunications Service Priority Provisioning and Restoration of Service

The provisioning and restoration of service in emergencies shall be in accordance with Part 64, Subpart D, Appendix A of the Federal Communications Commission's Rules and Regulations which specifies the prioritization for such activities.

3.17 Inspection

The Company may, upon reasonable notice, make such tests and inspections, as may be necessary to determine that the requirements of this tariff are being complied with in the installation, operation, or maintenance of the Customer's service. The Company may interrupt the type service at any time, without penalty to the Company, because of departure from any of these requirements.

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3. Rules and Regulations (cont'd)

3.18 Cancellation for Cause by the Company (See Section 3.3 for cancellation by customer)

3.18.1 The Company may discontinue the furnishing of any and/or all service(s) to a Customer, without incurring any liability, immediately and without notice if the Company deems, in its sole discretion, that such action is necessary to prevent or to protect against fraud or to otherwise protect its personnel, agents, facilities or services. The Company may discontinue service pursuant to this subsection if:

(a) The Customer refuses to furnish information to the Company regarding the Customer's creditworthiness, its past or current use of common carrier services, or its planned use of service(s);

(b) The Customer provided false information for the Company regarding the Customer's identity, address, creditworthiness, past or current use of common carrier communications services, or its planned use of Company service(s);

(c) The Customer states that it will not comply with a request by the Company for security for the payment for service(s) in accordance with Section **3.13.7** above or either the Customer has been given written notice by the Company of any past due amount (which remains unpaid in whole or in part) for any of the Company's services to which the Customer subscribes or had subscribed or used:

(d) The Customer either a) accesses the Company service by dialing the Company's Carrier Identification Code (CIC), or b) having presubscribed to the Company's service has had its account(s) canceled and has been removed from the Company's billing system and is being billed for its subsequent use of the Company's network by the local exchange carrier, and either refuses to pay when billed for the Company service(s) or indicates to the Company or its billing agent that it will not pay for Company service(s) used by it; or

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3. Rules and Regulations (cont'd)

3.18 Cancellation for Cause by the Company (cont'd)

3.18.1 (cont'd)

(e) A subscriber to the Company who accesses the service by use of an authorization code has not used the service (with the exception of calls to Directory Assistance) for ninety (90) days;

(f) Upon written notice to the Customer's billing address or notice to the Customer who is a subscriber to the Company's Calling Card service who has not used the service (with the exception of calls to Directory Assistance) for one-hundred eighty (180) days. In such case, the Company may deactivate the Customer's card to reduce the risk of unauthorized use. If the Customer wishes to renew usage of the service (e.g. upon returning from a vacation home), the Company will promptly supply a new card;

(g) The Customer uses service to transmit a message, locate a person or otherwise give or obtain information without payment for the service:

(h) The Customer uses, or attempts to use, service with the intent to avoid the payment, either in whole or in part, of the tariff charges for the service:

(1) Using or attempting to use service by rearranging, tampering with, or making connections to the Company's service not authorized by this tariff;

(2) Using tricks, schemes, false or invalid numbers, false credit devices, electronic devices, or any other fraudulent means or devices.

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3. Rules and Regulations (cont'd)

3.18 Cancellation for Cause by the Company (cont'd)

3.18.2 Upon written notice to the Customer of any sum thirty (30) days past due, the Company may immediately cancel service pursuant to this section; or

3.18.3 Immediately upon written notice to the Customer, after failure of the Customer to comply with a request by the Company for security for the payment of service in accordance with Section **3.13.7** above for five (5) days after sending the Customer written notice of noncompliance with any provision of this tariff if the noncompliance is not corrected within that five (5) day period, the Company may immediately cancel service pursuant to this section; or

3.18.4 The Company may, without notice, cancel service pursuant to this section without notice, if the Customer's account has shown no usage for six (6) consecutive months;

3.18.5 The discontinuance of service(s) by the Company pursuant to this Section does not relieve the Customer of any obligation to pay the Company for charges, dues and owings for service(s) furnished up to the time of discontinuance. In the event the Company cancels the Customers service for cause, and the Customer is committed to a term or other plan for which charges apply the Customer will be obligated to pay, as though it had terminated service early for its own convenience.

3. Rules and Regulations (cont'd)

3.19 Testing and Adjusting

Upon reasonable notice, the service provided by the Company shall be made available to the Company for such tests and adjustments as the Company deems necessary to maintain it in satisfactory condition.

3.20 Terminal Equipment

3.20.1 Terminal equipment, such as teleprinters, handsets, or data sets at the premises of the Customer and between such premises and the Company terminals, shall be furnished by and maintained at the expense of the Customer, except as otherwise provided.

3.20.2 The characteristics of equipment at either end of the channel shall be such that its connection to the channel complies with the minimum protection criteria set forth below, and does not interfere with services furnished to other Customers. Additional protective equipment, where required, shall be provided and maintained at the Customer's expense.

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3. Rules and Regulations (cont'd)

3.20 Terminal Equipment (cont'd)

3.20.3 When services using local exchange carrier voice grade facilities are terminated in Customer-provided terminal equipment, channel derivation devices, or communications systems, the Customer shall comply with the minimum protective criteria set forth below.

3.20.3.1 When the facilities furnished under this tariff are used in common with local exchange carrier services, it is necessary, in order to prevent excessive noise and crosstalk, that the power of the signal applied to local exchange lines be limited. A single valued limit for all applications cannot be specified. Therefore, the power of the signal in the band above 300 Hertz which may be applied by the Customer-provided equipment at the point of termination will be specified by the Company for each application.

3.20.3.2 To protect the telecommunications services from interference at frequencies which are above the band of service provided, the Company will specify the acceptable signal power in the following bands to be applied by the Customer-provided equipment or communications systems at the point of termination to insure that the input to local exchange carrier facilities does not exceed the limits indicated:

(a) The power in the band from 3995 Hertz to 4005 Hertz shall be at least 18 dB below the power of the signal as specified in Section **3.20.4**

(b) The power in the band from 4000 Hertz to 10,000 Hertz shall not exceed 16 dB below one milliwatt.

(c) The power in the band from 10,000 Hertz to 25,000 Hertz shall not exceed 24 dB below one milliwatt.

(d) The power in the band from 25,000 Hertz to 40,000 Hertz shall not exceed 36 dB below one milliwatt.

(e) The power in the band above 40,000 Hertz shall not exceed 50 dB below one milliwatt.

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3. Rules and Regulations (cont'd)

3.20 Terminal Equipment (cont'd)

3.20.4 Where in connection via Customer-provided terminal equipment or communications systems to a Message Telecommunications Service or a WATS service, to prevent the interruption or disconnection of a call, or interference with network control signaling, it is necessary that the signal applied by the Customer-provided equipment to the interface at no time have energy solely in the 2450 Hertz to 2750 Hertz. If signal is in the 2450 to 2750 Hertz, it must not exceed the power present at the same time in the 800 to 2450 Hertz Band.

3.20.5 Where such Customer-provided equipment or communications systems applies signals having components in the spectrum 300 Hertz, excluding ringing signals, the currents and voltages (including all harmonics and spurious) at the interface shall not exceed the limits indicated in Sections 3.20.5.1 through 3.20.5.4 following:

3.20.5.1The maximum rms. (root-means-square) value, including DC and AC components, of the current per conductor will not exceed .035 ampere.

3.20.5.2The magnitude of the peak of the conductor or ground voltage shall not exceed 70 volts.

3.20.5.3The conductor voltage shall be such that the conductor ground voltage limit in .10 proceeding is not exceeded. If the signal source is not grounded, the voltage limit in .0342 preceding applies to the conductor to conductor voltage.

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3. Rules and Regulations (cont'd)

3.20 Terminal Equipment (cont'd)

3.20.5 (cont'd)

3.20.5.4The total weighted rms. Voltage within the band from 50 Hertz to 300 Hertz shall not exceed 100 volts. The total weight rms. Is the square root of the sum of the products times the square of the rms. Voltage of the individual frequency components.

3.20.5.5The weighting factors are as indicated:

For Frequencies Between	Weight Factor
50 Hertz and 100 Hertz	f 2/104
100 Hertz and 300 Hertz	f33/106.6

3.20.5.6The Customer is responsible for all costs, which may include the expenses of Customer personnel, electrical power, etc. at the Customer's premises in the provision of the service described herein.

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3. Rules and Regulations (cont'd)

3.21 Systems Security (cont'd)

3.21.1 Where Customers are permitted access to the Company's computer systems and date for the purpose of managing and maintaining their telecommunications services, they will comply with the following:

(a) Customers may access the Company's systems only to the extent required by an incident to administer and manage the Customer's telecommunications systems.

(b) Customers may not disclose or use information which may be learned as a consequence of access to Company systems except as may be directly required to ensure the proper operations of the Customer's telecommunications systems. Customers must take all reasonable precautions to prevent any other person or entity who does not have a need to know from acquiring such information.

(c) Customers shall not in any manner or form disclose, provide, or otherwise make available, in whole or in part, Company documentation, any related material or any other confidential material except to those who have a need to know incident to the use of Company services. All documentation shall remain the property of the Company and may not be copied, reproduced, or otherwise disseminated without the prior written permission of the Company.

(d) Customers shall take all responsible precautions to maintain the confidentiality of all Company documents. Such precautions shall include the use of Personal Identifications Numbers (PINs) and passwords selected by and known only to the Customer's individual authorized users. Company telephone numbers and dial-up access number(s) assigned to Customers by the Company, PINs, or any aspect of access and sign-on methodology shall not be posted or shared with others under any circumstances. Customers shall follow normal logoff procedures prior to leaving a terminal unattended. Customers should report any known or suspected attempt by others to gain unauthorized access.

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3. Rules and Regulations (cont'd)

3.21 Systems Security

3.21.2 In the event that a security access device assigned to a Customer for dial-up access is lost, stolen, or misplaced, the Customer must notify the Company immediately. Access to information beyond that authorized may result in civil and/or criminal penalties.

3.22 Allowance for Interruptions

3.22.1 Except as provided for in Section **3.5** above, which pertain to Directory Assistance, the following credit allowances for interruptions of Company services will be made:

(a) Except as provided , for elsewhere in this tariff, credit allowances will be made for interruptions associated with those Company services for which charges are specified on the basis of per minute of use, or on usage of a fraction of a minute, and in which there may be interruption of an individual call, due to a condition in the Company's shared interexchange facilities or in shared access or termination facilities provided by other carriers, where the interruption can be remedied by redialing the calls. A credit allowance will be made for that portion of a call which is interrupted due to poor transmission (e.g. noisy circuit) quality, one-way transmission (one party is unable to hear the other) or involuntary disconnection caused by deficiencies in the Company's service. A Customer may also be granted credit for reaching a wrong number. To receive a credit, the Customer must notify a Company Customer Service Representative and furnish information, including the called number, the service subscribed to, the difficulty experienced, and the approximate time the call was placed, Credit allowances will not be made for a) interruptions not reported to the Company within twenty-four (24) hours, or b) interruptions that are due to the failure of power, equipment, systems, or services not provided by the Company. If the Customer elects to use another means of communications after one of the above interruptions, or during a period when he or she is unable to place a call over the Company, the Customer must pay the charges for the alternative service used.

3. Rules and Regulations (cont'd)

3.22 Allowance for Interruptions (cont'd)

3.22.1 (cont'd)

(b) An interruption period begins when the Customer reports to the Company that the service has been interrupted and releases it for testing and repair. An interruption period ends when the service is operative again. If the Customer reports the service to be inoperative but declines to release it for testing and repairs, the service is deemed to be impaired, but not interrupted. The Company may deny a Customer's request for credit where notification of alleged inferior, or inadequate service has not been received by the Company's Customer Service Department within twenty-four (24) hours of the occurrence. Credit will be allowed only for disabled portions of the service.

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3. Rules and Regulations (cont'd)

3.22 Allowance for Interruptions (cont'd)

3.22.1 (cont'd)

(c) Where a call has been disconnected, the Customer will be given a credit allowance equivalent to the charge for the initial minute of the call made to reestablish communications with the other party. Where a call has been interrupted by poor transmission or one-way transmission, the Customer will be given a credit allowance equivalent to the charge for the initial minute of a call made to continue communicating with the other party to the interrupted call. A Customer who has reached a wrong number will be given a credit allowance to the charge for the initial minute of the wrong number if he or she reports the situation, within twenty-four (24) hours to a Company Customer Service Representative.

(d) For all of the Company's services which involve dedicated access, dedicated interexchange transmission and/or dedicated termination, for which monthly recurring charges are applied, which are interrupted for more than an individual call and cannot be remedied by redialing the call except as provided in Section **3.24** below, the Customer will be given a credit allowance for an interruption of two consecutive hours or more, in accordance with the following:

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3. Rules and Regulations (cont'd)

3.23 Outage Credit

3.23.1 For the purpose of this tariff, all months contain thirty (30) days. Services offered by the Company are on a twenty-four (24) hours per day, seven (7) days per week basis unless specifically stated otherwise.

3.23.2 For purposes of credit computations, every month shall be considered to have seven hundred twenty (720) hours.

3.23.3 The Customer shall be credited for an interruption of service on a prorated basis for the facilities affected for each period of two (2) hours or additional major fraction thereof. The prorated credit will be based on the monthly recurring charge of the affected Company circuit(s).

3.23.4 No credit allowance will be made for:

a) Interruptions by the negligence of the Customer or others authorized by the Customer to use the Customer's service.

b) Interruptions due to the failure of power, equipment, systems, or service not provided by the Company.

c) Interruptions during any period during which the Company or its agents are not afforded access to the premises where access lines are associated with the Customer's service are terminated.

d) Interruptions during any period when the Customer or user has released the service to the Company for maintenance or rearrangement purpose, or for the installation of a Customer order.

e) Interruptions during the period when the Customer elects not to release the service for testing or repair and continues to use it on an impaired basis.

f) Non-completion of calls due to network busy conditions or interruptions not reported to the Company.

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3. Rules and Regulations (cont'd)

3.24 Interconnection with Other Carriers

3.24.1 Service furnished by the Company may be connected with services or facilities of another participating carrier. Such interconnection may be made at a Company terminal or entrance site, at a terminal of another participating carrier, or at the premises of a Customer, joint user, or authorized user. Service furnished by the Company is not part of a joint undertaking with other such carriers.

3.24.2 Any special interface equipment or facilities necessary to achieve compatibility between the facilities of the Company and other participating carriers shall be provided at the Customer's expense. Upon Customer request and acting as the Customer's authorized agent, the Company, in its discretion, may attempt to make the necessary arrangements for such interconnections.

3.24.3 Service furnished by the Company may be connected with our facilities or services of other participating carriers under the terms and conditions of the other participating carriers' tariffs applicable to such connections.

3. Rules and Regulations (cont'd)

3.25 Special Construction

Subject to the arrangement of the Company and to all of the regulations contained in this tariff, special construction of facilities may be undertaken on a reasonable effort basis at the request of the Customer. Special construction is that construction undertaken that:

(a) where facilities are not presently available, and there is no other requirement for the facilities so constructed;

(b) of a type other than that which the Company would normally utilize in the furnishing of its services;

(c) over a route other than that which the Company would normally utilize in the furnishing of its services;

(d) in a quantity greater than that which the Company would normally construct;

(e) on an expedited basis;

(f) on a temporary basis until permanent facilities are available;

(g) involving abnormal costs; or

(h) in advance of its normal construction.

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3. Rules and Regulations (cont'd)

3.26 Third Party Marketing Promotion

3.26.1 The Company may from time to time enter into agreements with third parties to market Company services. These promotions will be approved by the Florida Public Services Commission with specific starting and ending dates. Subsequent to entering into such agreements, the Company may pay commission to the third party marketing entity for qualifying monthly usage revenues generated by the Company Customers to whom the third party has marketed Company service(s). The actual level of commissions to be paid will be dependent on the nature and extent of activities engaged in by the third party on the Company's behalf, including, without limitation, initial sales efforts, order coordination and processing, customer service, service problem determination and resolution, billing coordination, billing dispute resolution, and the collection or guarantee of collection of the amounts billed to the Company Customers enrolled by the third party. The commission payments may be remitted by the third party, in whole or in part, and in its sole discretion, to Customers to whom it has marketed Company service(s).

3.26.2 Within a Third Party Marketing Promotion, the Company may waive its portion of installation charges on voice and data basic digital service and switched services until such time as the Customers DAL services is installed and made available.

3.27 Dedicated Service

3.27.1 Upon request and signing up for one of the Company's dedicated access line services (DAL), the DAL Customer will have the option of utilizing one of the Company's switched services until such time as the Customer's DAL service is installed and made available.

3.27.2 The Company will then credit the Customer the difference between the switched product rates and the applicable DAL rates after the DAL service is installed and in billing. The credit would only be for the period beginning with the first date the Customer is willing to accept installation of the DAL and the actual date the DAL is installed. The credit will be given on the Customer's second month's DAL bill received from the Company.

3. Rules and Regulations (cont'd)

3.28 Schools and Libraries Discount Program

3.28.1 General

The Schools and Libraries Discount Program permits eligible schools (public and private, grades Kindergarten through 12) and libraries to purchase the Company services offered in this tariff at a discounted rate, in accordance with the Rules adopted by the Federal Communications Commission (FCC) in its Universal Service Order 97-157, issued May 8, 1997. The Rules are codified at 37 Code of Federal Regulation (C.F.R.) 54.500 et. seq.

As indicated in the Rules, the discounts will be between 20 and 90 percent of the pre-discount price, which is the price of services to schools and libraries prior to application of a discount. The level of discount will be based on an eligible school or library's level of economic disadvantage and by its location in either an urban or rural area. A school's level of economic disadvantage will be determined by the percentage of its students eligible for participation in the national school lunch program, and a library's level of economic disadvantage will be calculated on the basis of school lunch eligibility in the public school district in which the library is located. A non-public school may use either eligibility for the national school lunch program or other federally approved alternative measures to determine its level of economic disadvantage. To be eligible for the discount, schools and .libraries will be required to comply with the terms and conditions set forth in the Rules. Discounts are available only to the extent that they are funded by the federal universal service fund. Schools and libraries may aggregate demand with other eligible entities to create a consortium.

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3. Rules and Regulations (cont'd)

3.28 Schools and Libraries Discount Program (cont'd)

3.28.2 Regulations

Obligation of eligible schools and libraries:

3.28.2.1Requests for service:

(a) Schools and libraries and consortia shall participate in a competitive bidding process for all services eligible for discounts, in accordance with any state and local procurement rules.

(b) Schools and libraries and consortia shall submit requests for services to the Schools and Libraries Corporation, as designated by the FCC, and follow established procedures.

(c) Services requested will be used for educational purposes.

(d) Services will not be sold, resold or transferred in consideration for money or any other thing of value.

3.28.2.2Obligations of the Company:

(a) The Company will offer discounts to eligible schools and libraries on commercially available telecommunications services contained in this tariff.

(b) The Company will offer services to eligible schools, libraries, and consortia at prices no higher than the lowest price it charges to similarly situated non-residential Customers for similar services (lowest corresponding price).

(c) In competitive bidding situations, the Company may offer flexible pricing or rates other than in this tariff, where flexible pricing arrangements are allowed.

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3. Rules and Regulations (cont'd)

3.28 Schools and Libraries Discount Program (cont'd)

3.28.3 Discounted Rates for Schools and Libraries

3.28.3.1 Discounts for eligible schools and libraries and consortia shall be set as a percentage from the pre-discount price, which is the price of services to schools and libraries prior to the application of a discount.

3.28.3.2 The discount rate will be applied to all commercially available telecommunications services purchased by eligible schools, libraries or consortia.

3.28.3.3 The discount rate is based on each school or library's level of economic disadvantage as determined in accordance with the FCC Order or other federally approved alternative measures (as permitted by the Rules) and by its location in either urban or rural area.

3.28.3.4 The discount matrix for eligible schools, libraries, and consortia can be found below in Section **3.28.4** of this tariff.

3.28.4 Schools and Libraries Discount Matrix

% Of Students Eligible For National School Lunch Program	% Of US Schools	Urban Discount	Rural Discount
<1%	3%	20%	25%
1% - 19%	31%	40%	50%
20% - 34%	19%	50%	60%
35% - 49%	15%	60%	70%
50% - 74%	16%	80%	80%
75% - 100%	16%	90%	90%

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4. Domestic Services

4.1 1+ Outbound

4.1.1 Switched Access

Switched access service is available to Customers for their use in furnishing their services to end users, provides a two-point communications path between a Customer's premises and an end user's premises. It provides for the use of common terminating, switching and transport facilities. Switched access service provides the ability to originate calls from an end user's premises location to an end user's premises.

Rates and charges are will be provided at a later date.

4.2 Toll Free Service

4.2.1 Switched Access
4.2.2 Dedicated Access

4.3 Saved for future use

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4. Domestic Services (cont'd)

4.4 Prepaid Calling Card

Prepaid Cards allow customers to acquire cards that are used to originate outbound direct dial calls via NEXTLINK toll-free numbers. Prepaid cards are available in various dollar denominations at the per minute rates set forth below. To use the card, callers must dial an access number. When the call is acknowledged, the caller then enters the PIN. At this point, the caller is notified of the dollar value remaining on the card. The caller then enters the telephone number to be called.

NEXTLINK will offer consumers the ability to purchase its prepaid cards in various dollar denominations. Each prepaid card will remain active until such time as the charges (as set forth below) equal the dollar value of the prepaid card purchased by the end-use or until the card expires (as set forth below).

4.4.1 Rate Per Minute Use:

The following per minute of use rates will apply in addition to the charges set forth in 4.4.2 through 4.4.3 below (as applicable).

	Option A	Option B	Option C
Rate Per Minute of Use	$0.039	$0.049	$0.079

4.4.2 Per Call Surcharge:

The following surcharge will be assessed on each call made (regardless of the length of the call or location from which the call is made) using a NEXTLINK prepaid card under Options A, B or C which originates in the contiguous United States and the following non-contiguous U.S. regions; including Alaska, Hawaii, Puerto Rico, U.S. Virgin Islands, Guam, Northern Marianas and American Samoa.

	Option A	Option B	Option C
Each Call	$0.49	$0.49	$0.59

4. Domestic Services (cont'd)

4.4 Prepaid Calling Card (cont'd)

4.4.3 Payphone Surcharge:

The following surcharge will be assessed on each call made (regardless of the length of the call) from a payphone using a NEXTLINK prepaid card under Options A, B or C which originates in the contiguous United States and the following non-contiguous U.S. regions; including Alaska, Hawaii, Puerto Rico, U.S. Virgin Islands, Guam, Northern Marianas and American Samoa

	Option A	Option B	Option C
Each Call	$0.30	$0.30	$0.30

4.4.4 Expiration of Prepaid Cards

NEXTLINK's prepaid cards will expire on the date specified on the card or package in which the card is included.

4.4.5 Directory Assistance

A charge of $1.25 will be assessed for each call requesting Directory Assistance.

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4. Domestic Services (cont'd)

4.4 Prepaid Calling Card (cont'd)

4.4.6 Conditions of Service

A. Only the entity in whose name the original qualifying purchase was made shall be deemed to be the Customer. Related entities, such as affiliates and subsidiaries, spouses and relatives, shall not be treated as the customer.

B. Calls to 500, 700, 800, 877, 888, 900 and 950 numbers will not be completed using the NEXTLINK prepaid card.

C. Neither NEXTLINK nor any of its authorized agents or contractors shall be liable or responsible for theft, loss or unauthorized use of any NEXTLINK prepaid cards or card numbers. NEXTLINK will not refund or issue credit for any unused value on any NEXTLINK prepaid card.

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