KELLEY DRYE & WARREN LLP
A LIMITED LIABILITY PARTNERSHIP

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VIA UPS

Florida Public Service Commission
Division of the Commission Clerk and Administrative Services
240 Shumard Oak Boulevard
Tallahassee, FL 32399

050907-TX
050908-TI

Re: Application of LMDS Holdings, Inc. for Authority To Provide Alternative Local Exchange Service and Registration to Provide Interexchange Services Within the State of Florida

Dear Sir or Madam:

Enclosed please find, for filing, one original and six (6) copies of the abovementioned Application and Registration. Please note that ***Exhibit B*** of the Application contains sensitive, confidential and proprietary financial information. Accordingly, LMDS Holdings, Inc. ("Holdings") respectfully requests that ***Exhibit B*** is filed under seal.

Please date-stamp the duplicate of this filing and return in the self-addressed, postage prepaid envelope. Thank you for your assistance in this matter and please do not hesitate to contact me at (202) 955-9669 if you have any questions or concerns.

Respectfully submitted,

Katherine E. Barker Marshall

Katherine E. Barker Marshall

Enclosures Original Price List forwarded to CCP

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

DIVISION OF COMPETITIVE MARKETS AND ENFORCEMENT CERTIFICATION

050907-TX

APPLICATION FORM
for
AUTHORITY TO PROVIDE
ALTERNATIVE LOCAL EXCHANGE SERVICE
WITHIN THE STATE OF FLORIDA

Instructions

- This form is used as an application for an original certificate and for approval of the 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 Page 12).

- 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 the Commission Clerk and Administrative Services
  2540 Shumard Oak Blvd.
  Tallahassee, Florida 32399-0850
  (850) 413-6770

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

  Florida Public Service Commission
  Division of Competitive Markets and Enforcement Certification
  2540 Shumard Oak Blvd.
  Tallahassee, Florida 32399-0850
  (850) 413-6600

APPLICATION

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

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

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

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

   (   ) **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:**
   LMDS Holdings, Inc.

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

   LMDS Holdings, Inc.

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

   11111 Sunset Hills Road
   Reston, VA 20190-5339

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

Corporation Service Company
1201 Hayes Street
Tallahassee, FL 32301

6. **Structure of organization:**

( ) Individual	( ) Corporation
(√) Foreign Corporation	( ) Foreign Partnership
( ) General Partnership	( ) Limited Partnership
( ) Other	

7. **If individual, provide:**

Name: Not applicable

Title:

Address:

City/State/Zip:

Telephone No.:_________________________ Fax No.:

Internet E-Mail Address:

Internet Website Address:

8. **If incorporated in Florida, provide proof of authority to operate in Florida:**

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

9. **<u>If foreign corporation,</u> provide proof of authority to operate in Florida:**

(a) The Florida Secretary of State corporate registration number: F05000009665.

10. **<u>If using fictitious name-d/b/a,</u> provide proof of compliance with fictitious name statute (Chapter 865.09, FS) to operate in Florida:**

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

Not Applicable

11. **<u>If a limited liability partnership</u>, provide proof of registration to operate in Florida:**

(a) The Florida Secretary of State registration number:

Not Applicable

12. **<u>If a partnership</u>, provide name, title and address of all partners and a copy of the partnership agreement.**

Name: Not Applicable

Title:

Address:

City/State/Zip:

Telephone No.:______________________ Fax No.:

Internet E-Mail Address:

Internet Website Address:

13. **<u>If a foreign limited partnership,</u> provide proof of compliance with the foreign limited partnership statute (Chapter 620.169, FS), if applicable.**
Not Applicable

(a) The Florida registration number:

14. Provide F.E.I. Number(if applicable): 91-2008276

15. 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. Provide explanation.

No.

(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.

All of the officers of LMDS Holdings, Inc. are also officers of XO Communications Services, Inc., which was certificated by this Commission to provide local exchange services in Docket No. 980470-TX issued 6/13/98 and interexchange services in Docket No. 980472-TI issued 5/22/98.

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

(a) The application:

Name: Katherine E. Barker Marshall, Esq.

Title: Counsel to LMDS Holdings, Inc.

Address: Kelley Drye and Warren, LLP; 1200 19th Street NW, Suite 500

City/State/Zip: Washington, DC 20036

Telephone No.: (202) 955-9669 Fax No.: (202) 955-9792
Internet E-Mail Address: **kbarker@kelleydrye.com**

Internet Website Address: www.kelleydrye.com

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

Name: David LaFrance

Title: Regulatory and External Affairs
Address: 11111 Sunset Hills Road

City/State/Zip: Reston, VA 20190

Telephone No.: (703) 547-2682 Fax No.: (703)547-2881

Internet E-Mail Address: David.LaFrance@xo.com

Internet Website Address: www.xo.com

(c) Complaints/Inquiries from customers:

Name: Tamie Whitefoot

Title: Customer Care Manager

Address: 4800 Concentric Blvd.

City/State/Zip: Saginaw, MI 48604

Telephone No.: (877) 714-6398 Fax No.: (989) 758-6510

Internet E-Mail Address: **cr-snaops@xo.com**

Internet Website Address: Applicant is in the process of building its website.

17. List the states in which the applicant:

(a) has operated as an alternative local exchange company.

Applicant has not operated as a local exchange company.

(b) has applications pending to be certificated as an alternative local exchange company.

Applicant has applications pending to provide local exchange service in the following jurisdictions: Alabama, Arizona, California, Colorado, Connecticut, District of Columbia, Florida, Georgia, Illinois, Indiana, Iowa, Kentucky, Maryland, Massachusetts, Michigan, Minnesota, Missouri, Nebraska, New Hampshire, New Mexico, New York, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, Texas, Washington and Wisconsin.

(c) is certificated to operate as an alternative local exchange company.

Applicant is not currently certificated to provide local exchange services in any jurisdiction.

(d) has been denied authority to operate as an alternative local exchange company and the circumstances involved.

Applicant has not been denied authority to operate as a local exchange carrier in any jurisdiction.

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

Applicant has not had any regulatory penalties imposed for violations of telecommunications statutes.

(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.

18. Submit the following:

A. Managerial capability: give resumes of employees/officers of the company that would indicate sufficient managerial experiences of each.

Please see ***Exhibit A.***

B. 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.

Applicant's management team includes individuals with substantive experience in successfully developing and operating telecommunications business. Consequentially, the Company has the adequate internal technical resources to support its Florida operations. This expertise in the telecommunications industry makes Applicant's management team well-qualified to operate its local exchange and interexchange operations in Florida. Specific details of the business and technical experience of Applicant's officers and management personnel are attached as ***Exhibit A***, which also contain biographies and a brief description of the business experiences of key management personnel who will be responsible for Applicant's telecommunications services in Florida and throughout the United States.

C. Financial capability.

The application **should contain** 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. **written explanation** that the applicant has sufficient financial capability to provide the requested service in the geographic area proposed to be served.

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

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

Applicant is a recently-formed entity, and as such does not have a significant financial history of its own, and has attached projected financial statements as ***Exhibit B, under seal***. Applicant will receive an additional infusion of capital once the transaction outlined below is completed.

Company has historically operated as a wholly owned subsidiary of XO Communications, Inc., a publicly traded company that has funded Applicant's operations. XO Communications, Inc.'s Securities and Exchange Commission Form 10K for the calendar years 2004 and 2005 are included as ***Exhibit C***.

XO Communications, Inc. is in the process of a *pro forma* restructuring merger. As a result of this restructuring, XO Communications, Inc. will be merged into XO Communications, LLC and removed from the ownership structure of Holdings.

This will leave XO Holdings, Inc. in the place of XO Communications, Inc. as parent-company to Holdings. Holdings will share the same ultimate owner with XO Communications, LLC, Carl C. Icahn. A notice of this transaction will be filed with the Commission under separate cover. A press release describing this transaction can be found at http://www.xo.com/news/278.html, a copy of which is attached as *Exhibit D.*

THIS PAGE MUST BE COMPLETED AND SIGNED

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

UTILITY OFFICIAL:

Carl J. Grivner
Print Name

Carl J. Grivner
Signature

Chief Executive Officer
Title

Date

(703) 547-2000
Telephone No.

(703) 547-2881
Fax No.

Address:

11111 Sunset Hills Road
Reston, VA 20190

THIS PAGE MUST BE COMPLETED AND SIGNED

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:

Carl J. Grivner
Print Name

Carl J. Grivner
Signature

Chief Executive Officer
Title

Date

(703) 547-2000
Telephone No.

(703) 547-2881
Fax No.

Address:

11111 Sunset Hills Road
Reston, VA 20190

Exhibit A

Management Biographies

Carl J. Grivner
President & Chief Executive Officer

Carl J. Grivner is Chief Executive Officer of XO Communications ("XO") and LMDS Holdings, Inc. ("Holdings").

Mr. Grivner's career in telecom and technology spans more than 25 years. He previously served as Chief Operating Officer at Global Crossing. Prior to joining Global Crossing in June 2000, Mr. Grivner served as Chief Executive Officer of Worldport Communications and before that, he served as Chief Executive Officer, Western Hemisphere, of Cable & Wireless PLC. Additionally, Mr. Grivner has held various senior executive positions at Advanced Fiber Communications and Ameritech. Mr. Grivner began his career working in sales at IBM. He also served in the United States Marine Corps from 1975-1978. He earned his Bachelor of Arts from Lycoming College.

Wayne Rehberger
Executive Vice President, Chief Operations Officer

Wayne Rehberger is chief operating officer of XO and Holdings. In this role he is responsible for all aspects of XO's operations including marketing, network and sales. He previously served as the company's chief financial officer for more than three years. During that time he led the company through a successful financial and operational restructuring that improved XO's operating metrics and financial performance through efficiency initiatives and the reduction of operating and overhead costs.

Mr. Rehberger has 20 years of diversified telecommunications management experience including having served in a number of executive roles at MCI Communications Corporation. During his time at MCI, Mr. Rehberger served in a variety of corporate and business unit accounting, finance, and operational support roles. He was involved in major acquisition activities, both from a business development and operational integration role. Mr. Rehberger held the position of senior vice president of Finance at MCI WorldCom prior to joining XO.

Prior to joining MCI, Mr. Rehberger served four years in the U.S. Army, achieving the rank of captain before joining KPMG's consulting practice in Washington, D.C. where he worked on various management consulting engagements focused on business strategy, marketing, and program/product management.

Bill Garrahan
Acting Chief Financial Officer and Senior Vice President, Corporate Development & Strategic Planning

Bill Garrahan is both acting Chief Financial Officer and Senior Vice President of Corporate Development at XO and Holdings. He oversees the company's financial functions and leads the company's mergers and acquisitions, corporate strategy and new business development activities. He joined the company in July 2001 as a senior member of its corporate development team, later playing a critical role in the company's acquisition of Allegiance Telecom.

Garrahan has nearly 20 years of experience in the telecommunications industry including previous positions at Lehman Brothers as a telecommunications equity analyst and MCI, where he held a variety of executive finance and business development functions, including Vice President of Corporate Planning and CFO of MCI's $6 billion consumer business unit.

Simone Wu
Senior Vice President, Acting General Counsel & Secretary

Simone Wu is acting General Counsel and Vice President at XO and Holdings. In this role, she oversees all of the company's legal affairs, which include commercial, corporate, employment, and intellectual property matters, as well as all litigation in which the Company is involved.

Wu has more than 16 years of wide-ranging experience in the telecommunications industry, including domestic and international business and corporate development, intellectual property and commercial matters, and legal and regulatory affairs. Prior to joining XO in 2001, Wu held business and legal positions at MCI and AOL among other places, and practiced domestic and international transactional and telecommunications law at the law firm of Skadden, Arps, Slate, Meagher & Flom.

She graduated with high honors from the University of Michigan with a degree in Political Science and as a Harlan Fiske Stone Scholar from Columbia University Law School.

Ron Scott
Vice President, Real Estate

Mr. Scott holds two senior executive titles at XO and Holdings and is currently responsible for XO's strategic business units and XO's national real estate portfolio. As Group President/CEO of XO One, XO Hosting and XO Interactive, Ron is charged with growing revenue profitably and strategically positioning these business units to maximize XO's core customer value proposition. Ron is also Senior Vice President of Real Estate responsible for managing XO's national real estate portfolio which includes building access and all company lease obligations.

Mr. Scott has over 20 years experience in the telecommunication services industry. Prior to joining XO, Ron co-founded Access Communications with the Trammell Crow family in Dallas, Texas. Access was a pioneer telecommunications startup that provided bundled telecommunication services to tenants in upscale commercial office properties. As President and CEO of Access Telecommunication Group, L.P., Ron spent 10 years growing this startup and ultimately led the transaction to sell the company to Shared Technologies. Upon the sale of his company, Ron served as Vice Chairman of the Board of Shared Technologies in West Hartford, Connecticut.

Prior to Mr. Scott's startup at Access, Ron held executive positions and led sales and marketing efforts in the cable industry. He was National Sales VP for CCX, Inc., a cable and connector manufacturer. Ron also spent several years as Director of Marketing and Sales for United Cable Television and Director of Sales for Cox Cable.

Mr. Scott was formerly on the Board of Directors for North American Telecommunication Association. In 1992 and 1993, Mr. Scott was recognized by the Southern Methodist University's Cox School of Business as CEO of the 11th and 25th fastest growing privately held company in the Dallas metropolitan area. Mr. Scott has a Bachelor's degree in Political Science from the University of North Texas.

Heather Burnett Gold
Senior Vice President, Government Relations

Heather Burnett Gold is Senior Vice President of Government Relations at XO and Holdings. In this role she oversees all of XO's advocacy with the federal government, including Congress, the FCC, other federal agencies, and the White House, and with state legislative and regulatory entities.

A telecommunications veteran with more than 20 years of experience, Gold joined XO from the KDW Group, where she was a co-founder & principal, providing strategic and financial planning to companies in the telecommunications industry with respect to opportunities created by regulatory change. Prior to The KDW Group, Gold was vice president of industry affairs at Intermedia Communications where she oversaw the company's regulatory, legislative and industry relations at both the state and federal levels. Before Intermedia, Gold served as president of the Association for Local Telecommunications Services (ALTS) from 1993 to 1998. During her tenure at ALTS, Gold was a leading proponent for opening local telecommunications markets to facilities-based competition and a driving force behind the Telecommunications Act of 1996. Before joining ALTS, she served as vice president of member services for the Competitive Telecommunications Association (CompTel).

Gold holds an MBA in marketing and finance from Washington University in St. Louis and Bachelors and Masters degrees in Economics from Tufts University.

Benjamin R. Preston
Corportate Counsel, Director of Legal Affairs & Assistant Secretary

Benjamin R. Preston is Principal Counsel, Corporate Development & Finance and Assistant Secretary of XO Communications, Inc. and LMDS Holdings, Inc. In this role, Mr. Preston handles all mergers & acquisitions, joint ventures, corporate finance, Securities & Exchange Commission reporting, and corporate governance matters at XO.

Mr. Preston has served in this capacity since January 2004. Prior to joining XO, Mr. Preston practiced corporate & securities law at Sidley Austin Brown & Wood LLP. He is a graduate of the University of Massachusetts at Amherst, Georgetown University Law Center, and McDonough

Graduate School of Business at Georgetown University.

Chet Kudtarkar
Vice President- Finance

Chet Kudtarkar has over 26 years of experience with over 18 years in the telecommunications industry. He has served in various financial management positions in the area of Planning, Analysis and Business Development. He also has experience in Marketing, Implementation and Program Management. In 1994 he was involved in the early stages of starting MCIMetro, a competitive local exchange carrier. With MCI, he was responsible for negotiating all interconnection agreements with incumbent local exchange companies. He has an extensive background in Financial Planning and Telco Cost management. Most recently, Kudtarkar has been the Director of Strategy and Corporate Development for XO Communications.

Chet Kudtarkar has an MBA from the Wharton School and a Masters in Engineering from the University of Mississippi.

Brad Magnuson
Director of Engineering

Brad Magnuson has over 15 years experience in design of public and private wireless telecommunications networks, metropolitan fiber based applications, and national IP infrastructures.

He has held various engineering management positions at XO Communications over the past ten years including District Director of Engineering for the Western Region where he designed CLEC networks in several western cities. He has also been involved in design of XO's national long haul fiber network, in development of its VoIP product and in its early technology trials of equipment operating in the LMDS spectrum. Prior to joining XO, Brad spent four years with a regional gas utility where he assisted in engineering a private microwave system carrying voice and telemetry applications across three western states. Brad currently serves as Director of Engineering for Fixed Wireless Applications within XO Communications.

Brad has a Bachelor of Science in Electrical Engineering from the University of Utah with emphasis in Microwave Engineering, Computer Engineering, and Digital Signal Processing in telecommunications systems.

Exhibit B

Projected Financial Statements

Confidential and Proprietary – Filed Under Seal

Exhibit C

XO Communications, Inc.

2003 and 2004 Form 10K Filings

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

FORM 10-K

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

For the fiscal year ended December 31, 2003

OR

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

Commission File No. 0-30900

XO COMMUNICATIONS, INC.
(Exact name of registrant as specified in its charter)

Delaware	54-1983517
(State or other jurisdiction of incorporation or organization)	**(I.R.S. employer identification no.)**

11111 Sunset Hills Road
Reston, Virginia 20190
(Address of principal executive offices, including zip code)

(703) 547-2000
(Registrant's telephone number, including area code)

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

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, par value $0.01 per share
(Title of class)

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 ☑ NO ☐

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

Indicate by check mark whether the Registrant is an accelerated filer (as defined by Rule 12b-2 of the Act.). YES ☑ NO ☐

The aggregate market value of the common stock held by non-affiliates of the Registrant, based upon the closing sale price of the common stock on June 30, 2003 (which is the last business day of the Registrant's second fiscal quarter), as reported on the Nasdaq Over-the-Counter Bulletin Board, was approximately $139 million. Shares of common stock held by each executive officer and director and by certain persons who own 5% or more of the outstanding 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.

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. YES ☑ NO ☐

Number of shares of common stock outstanding as of February 20, 2004: 136,510,535

DOCUMENTS INCORPORATED BY REFERENCE

Part III — Portions of the registrant's definitive proxy statement to be issued in conjunction with registrant's annual stockholders' meeting to be held on May 27, 2004.

TABLE OF CONTENTS

PART I

PART II

PART III

PART IV

PART I

Item 1. Business

This Annual Report on Form 10-K, including "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Item 7, contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause the results of XO Communications, Inc. or XO Parent and its consolidated subsidiaries or XO to differ materially from those expressed or implied by such forward-looking statements. All statements other than statements of historical fact are statements that could be deemed forward-looking statements, including any projections of earnings, revenue, synergies, accretion, margins, costs or other financial items; any statements of the plans, strategies and objectives of management for future operations, including the execution of integration and restructuring plans; any statement concerning proposed new products, services, developments or industry comparisons; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing. The risks, uncertainties and assumptions referred to above include the performance of contracts by vendors and customers; employee management issues; the challenge of managing asset levels, including inventory; the difficulty of aligning expense levels with revenue changes; and other risks that are described herein and that are otherwise described from time to time in XO's Securities and Exchange Commission reports including but not limited to the items discussed in "Business — Factors that Could Affect Future Results". XO assumes no obligation and does not intend to update these forward-looking statements.

Introduction

XO Communications, Inc., a Delaware corporation, is a leading independent broadband telecommunications services provider that markets a comprehensive array of telecommunications services, including local and long distance voice, Internet access, private data networking and hosting services.

The initial predecessor entity of XO Parent was formed as a Washington limited partnership in 1994. In 1995, that entity merged into a Washington limited liability company that became known as "NEXTLINK Communications, L.L.C." In January 1997, NEXTLINK Communications, L.L.C. merged into NEXTLINK Communications, Inc., a Washington corporation, which in June 1998 reincorporated in Delaware under the same name. On June 16, 2000, in connection with the acquisition of Concentric Network Corporation, NEXTLINK Communications, Inc. merged with and into a new corporation and that corporation, as the surviving corporation in the merger, changed its name to NEXTLINK Communications, Inc. On September 25, 2000, NEXTLINK Communications, Inc. began doing business as "XO Communications" and, on October 25, 2000, changed its name to XO Communications, Inc. We conduct our business primarily through the more than 70 subsidiaries that XO Parent owns and manages.

On June 17, 2002, XO Parent filed for protection under Chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the Southern District of New York. On November 15, 2002, the Bankruptcy Court confirmed XO Parent's plan of reorganization, and, on January 16, 2003, XO Parent consummated the plan of reorganization and emerged from its Chapter 11 reorganization proceedings with a significantly restructured balance sheet.

In December 2001, XO Parent voluntarily delisted its pre-petition class A common stock from the Nasdaq National Market, which was traded under the symbol "XOXO", and, on December 17, 2001, began trading on the Over-the-Counter Bulletin Board, or OTCBB. As of January 16, 2003, XO Parent's pre-petition class A common stock stopped trading on the OTCBB and all interests in XO Parent's pre-petition class A common stock were terminated pursuant to the plan of reorganization. The shares of common stock issued by the reorganized XO Parent pursuant to its plan of reorganization began trading in January 2003 on the OTCBB and in the Pink Sheets under the symbol "XOCM.OB" shortly after the first distribution of common stock pursuant to its plan of reorganization.

Our principal executive and administrative offices are located at 11111 Sunset Hills Road, Reston, Virginia 20190 and our telephone number is (703) 547-2000. Our Internet address is www.xo.com, where, under "About XO-Investor Center", you can find copies of our annual report on Form 10-K as of and for the year ended December 31, 2003, and our quarterly reports on Form 10-Q and current reports on Form 8-K, all of which we make available as soon as reasonably practicable after the report is filed with the Securities and Exchange Commission, or the Commission.

Overview of Our Company

The Telecommunications Act of 1996, or the "Telecom Act", which substantially revised the Communications Act of 1934, established the regulatory framework for the introduction of competition for local telecommunications services throughout the United States by new competitive independent entrants such as us. Prior to the passage of the Telecom Act, states typically granted an exclusive franchise in each local service area to a single dominant carrier — often a former subsidiary of AT&T known as a Regional Bell Operating Company ("RBOC") — which owned the entire local exchange network and operated a virtual monopoly in the provision of most local exchange services in most locations in the United States. The RBOCs, following some recent consolidation, now consist of the following companies: BellSouth, Verizon, Qwest Communications and SBC Communications.

We provide business customers with a comprehensive array of telecommunications services, including local and long distance voice, Internet access, private data networking and hosting services. Our services are designed to be provided through our network assets, which are capable of carrying high volumes of all types of telecommunications traffic. We market our services primarily to business customers, including small and middle-market businesses, Fortune 500 companies, and carrier and wholesale customers. Although our services benefit businesses of all sizes, we believe them to be of particular benefit to multi-location businesses that desire to improve telecommunications among their locations, whether within a single metropolitan area or across the country. Our services include the following:

1) Voice services:

- Local and long distance services, other voice-related services such as conferencing, domestic and international toll free services and voicemail, and transaction processing services for prepaid calling cards; and
- Hosted interactive voice response, or IVR, systems that we develop, host and manage that enable our customers' end-users to order products and services, collect and receive information, seek assistance, facilitate bill payment and a host of other capabilities over the telephone using natural language speech recognition and systems that enable persons to access web-based information over the telephone;

2) Data services:

- Internet access:
  - Dedicated Internet access for customers with large, high-speed Internet access requirements;
  - Digital subscriber line, or DSL, services for businesses that require high-speed Internet access over existing copper wire telephone lines; and
  - Dial access, which allows remote users to connect to XO's network;
- Private data networking:
  - Dedicated transmission capacity on our network, including dedicated circuits and the lease of one or more dedicated wavelengths on a fiber optic cable, to customers that desire high-bandwidth links between locations;
  - Virtual private network, or VPN, services, which provide customers with a managed, private data service over the public Internet, designed for medium and large businesses

that want to create secure, wide-area networks for users at various and remote locations; and

- Ethernet services, which are designed to connect the local area networks, or LANs, of medium and large customers within and between metropolitan areas at speeds of up to one gigabit per second;

- Hosting services:

  - Web site services, which allow a customer to establish a Web presence;

  - Web hosting, including hosting and web site traffic management tools, for Internet-centric businesses, and streamed media services designed for small and middle-market businesses; and

  - Server collocation and management and customer support to manage a customer's hosting needs; and

3) Integrated voice and data services

- Integrated, flat rate service packages that we refer to as XOptions. These packages eliminate the separation between local and long-distance telecommunications services, and combine our "all distance" telephone services with high-speed Internet access and web hosting services, all for one flat monthly rate.

- Shared tenant services, which are telecommunications management services provided to groups of small and middle-market business located in the same office building.

We believe that a significant factor considered by business customers in making the decision to purchase telecommunications services is the quality of service and customer support offered by the service provider. We focus on proactive resolution of customer issues by training our customer care representatives extensively on the services that we offer and promoting accountability of the customer care team. We also have developed a secure, on-line business center, through which many customers can access information about their accounts and track requests, review services, analyze trends, make decisions and pay bills.

To serve our customers' broad and expanding telecommunications needs, we utilize network assets located across the United States, substantially all of which we own or control through indefeasible exclusive rights or other leasing arrangements, making us a facilities-based carrier. Indefeasible exclusive rights are contracts with the owners of fiber optic cables that allow us to use a specified amount of capacity on a specified fiber on those cables for terms ranging from 10 to 25 years. Our network assets incorporate state-of-the-art fiber optic cable, dedicated wavelengths of transmission capacity on fiber optic networks and transmission equipment capable of carrying high volumes of data, voice, video and Internet traffic. We are able to provide a comprehensive array of telecommunications services primarily or entirely over our integrated network, from the initiation of the voice or data transmission to the point of termination. This capability enables us to provide "end-to-end" telecommunications services between customers connected to our network, and among a customer's multiple locations, primarily or entirely over our integrated network.

Our network consists of metro fiber networks located in the U.S. metropolitan areas that we serve, connected by our intercity network. Our metro fiber networks consist of rings of fiber optic cables encircling the central business districts of numerous metropolitan areas. We operate 37 metro fiber networks in 22 states and the District of Columbia, including 25 of the 30 largest metropolitan areas in the U.S. We have constructed, acquired or leased our metro fiber networks, each of which consists of up to 432 strands of fiber optic cable and, in some cases, empty conduits through which additional fiber optic cable can be deployed.

Our metro fiber networks are connected primarily by dedicated wavelengths of transmission capacity that we have obtained on intercity fiber optic cables, which we refer to as our intercity network. To deploy our intercity network, we have leased dedicated, high-capacity wavelengths of transmission capacity on fiber optic cables, onto which we have deployed our own switching, routing and optical equipment. We also hold indefeasible exclusive rights to use 18 fiber optic strands on the routes served by our intercity networks pursuant to arrangements with Level 3, substantially all of which are not currently in use, referred to in our industry as unlit. As a result, we have the ability to utilize significant additional network capacity as our business grows.

We hold licenses for 1,150 to 1,300 MHz of local multipoint distribution services, or LMDS, spectrum in 59 cities. Our licenses also include:

- 150 MHz of LMDS spectrum in 14 other cities;
- 150 MHz of LMDS spectrum in the five boroughs that comprise New York City (300 MHz total); and
- 400 MHz of LMDS spectrum in Denver.

We also hold ten broadband wireless licenses in the 39 GHz (gigahertz) frequency band, of which five provide from 100 to 300 additional MHz in two cities where we hold a 150 MHz LMDS license, plus 100 MHz in Denver and 200 MHz of spectrum in Las Vegas, where we do not hold a LMDS license.

Our Reorganization

From 1996 through 2001, XO Parent accumulated outstanding indebtedness in excess of $5 billion in connection with the financing and acquisition of our network. Following the decline in the market valuations of emerging telecommunications companies in 2001, we were unable to obtain additional funding for our operations and to support our outstanding indebtedness. As a result, despite reductions in our operating expenses, including a reduction in our workforce in 2001 from 7,400 to 6,712 employees, and the implementation of other cost control measures, we concluded that our cash on hand would not be sufficient to fund operations, capital expenditures and debt service until such time as we expected our operations to become profitable and we determined that a restructuring of our business was necessary.

On June 17, 2002, XO Parent filed for protection under the Bankruptcy Code. On November 15, 2002, the Bankruptcy Court confirmed XO Parent's plan of reorganization, and, on January 16, 2003, XO Parent consummated the plan of reorganization and emerged from its Chapter 11 reorganization proceedings with a significantly restructured balance sheet.

Implementation of the Plan of Reorganization

On January 16, 2003, our Effective Date, XO Parent consummated its Plan of Reorganization and emerged from its Chapter 11 reorganization proceedings with a significantly restructured balance sheet. The consummation of the Plan of Reorganization resulted in the following changes in XO Parent's capital structure:

- The conversion of $1.0 billion of loans under our pre-petition secured credit facility into $500.0 million of outstanding principal amount under an amended and restated secured credit agreement;
- The extinguishment of all amounts due under our pre-petition unsecured senior and subordinated notes and certain general unsecured obligations;
- The cancellation of all outstanding shares and interests in our pre-petition preferred stock and pre-petition common stock; and
- The issuance of approximately 95.0 million shares of new common stock in reorganized XO and warrants to purchase up to an additional 23.75 million shares of New Common Stock of reorganized XO.

The following table shows the distribution each party of interest impacted by XO Parent's bankruptcy was entitled to. As certain claims are still being reviewed by the Bankruptcy Court, certain proportional distributions have not yet been made and can not occur until the court rules (dollars in thousands, except share data).

Party of Interest	Shares of New Common Stock	Series A Warrants	Series B Warrants	Series C Warrants	Credit Facility	Cash
$1 Billion senior secured credit facility	90,250,001	—	—	—	$500,000	$ —
Senior unsecured notes	4,715,344	9,430,689	7,073,015	7,073,015	—	1,600
Subordinated notes	—	—	—	—	—	616
General unsecured creditors	34,656	69,309	51,980	51,980	—	403
Total entitlement	95,000,001	9,499,998	7,124,995	7,124,995	$500,000	$2,619
Not yet distributed	1,230,638	2,461,743	1,846,151	1,846,151	—	1,612
Total issued or paid	93,769,363	7,038,255	5,278,844	5,278,844	$500,000	$1,007

As part of our Plan of Reorganization, we agreed to initiate a Rights Offering that allowed certain holders of claims and interests in XO Parent as of the November 15, 2002 record date to subscribe for up to 40.0 million shares of New Common Stock at $5.00 per share. The Rights Offering closed on January 5, 2004. An aggregate of 39.7 million shares were issued, yielding net proceeds of $197.6 million. Subsequent to closing, these proceeds were used to pay down our Credit Facility from $536.8 million at December 31, 2003 to approximately $339.2 million.

Interests Held by Entities Controlled by Mr. Carl C. Icahn

Various entities controlled by Mr. Carl C. Icahn, Chairman of XO Parent, hold the following interests in reorganized XO:

	Common Stock	Series A, B and C Warrants	Credit Facility
At December 31, 2003	Greater than 80%	Greater than 40%	Greater than 90%
At January 31, 2004	Greater than 60%	Greater than 40%	Greater than 90%

In addition entities controlled by Mr. Icahn have acquired an option to purchase 6.25 million additional shares of common stock from Franklin Mutual Advisors, LLC at a strike price of $4.25 per share which expires June 21, 2004. After closing our rights offering in January 2004, Mr. Icahn's ownership interest in our outstanding common stock was reduced to over 60%. On January 27, 2004, Icahn and Associates filed a Form 13D with the Securities and Exchange Commission stating they held beneficial ownership as defined therein of 69% of XO Parent.

Accounting Impact

As a result of the consummation of the Plan of Reorganization, XO Parent was required to implement the fresh start accounting provisions of SOP 90-7 "Financial Reporting by Entities in Reorganization Under the Bankruptcy Code" to its financial statements. The fresh start accounting provisions required that we establish a "fair value" basis for the carrying value of the assets and liabilities for Reorganized XO.

For further discussion of the effects of our implementation of the Plan of Reorganization on our financial condition and results of operations, see "Our Chapter 11 Reorganization" and "Liquidity and Capital Resources" in "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Acquisition of Assets of Allegiance Telecom, Inc.

On February 19, 2004, the United States Bankruptcy Court for the Southern District of New York approved the Asset Purchase Agreement by and between XO Parent and Allegiance Telecom, Inc., or Allegiance, pursuant to which we have agreed to acquire substantially all of the assets of Allegiance for approximately $311.0 million in cash and approximately 45.4 million shares of our New Common Stock. We anticipate we will receive the required governmental approval prior to or shortly after the beginning of the second quarter of 2004. At that point in time, we will operate under a management agreement whereby the combined management team will exercise day to day operating control over the assets and operations to be acquired from Allegiance. We anticipate that our acquisition of the Allegiance assets will be consummated during the third quarter of 2004 after all other federal and state regulatory approvals are obtained.

The Allegiance assets consist primarily of:

- switching and routing equipment, located both in current Allegiance facilities and in facilities operating by one or more incumbent local exchange carriers;
- physical points of presence in the form of network operations centers, data centers, central offices, and sales offices located in 36 major metropolitan areas;
- customer and sales agreements that constitute a majority of Allegiance's voice and data revenues;
- leased intercity and metro fiber network capacity that is both redundant to and expansive of our current network; and
- billing, provisioning, and other back-office information technology platforms.

With the acquisition of substantially all of Allegiance's network assets and customer base, XO will become one of the nation's largest competitive independent providers of national local telecommunications and broadband services with approximately 250,000 customers and approximately $1.6 billion in annual revenues. We will own one of the largest network of nationwide connections to the RBOC's networks, and will double our Points of Presence (PoPs) within the 36 metropolitan areas where both XO and Allegiance operate. XO believes that this extensive network will allow XO to (i) improve delivery of service to customers (ii) reduce network costs (iii) improve operating results and (iv) improve our ability to compete with other companies in the nationwide local telecommunications services market. In addition, the combination of XO and Allegiance will enhance the strength and depth of the combined human resource team by combining the sales, technical and management expertise of both companies.

Based on information made available to us by Allegiance, we estimate the annual revenue associated with the operations that we will acquire will exceed $500.0 million. Allegiance's filings with the Securities and Exchange Commission can be found on their web site www.allegiancetelecom.com. We believe that we will be able to realize network operations and selling, operating, and administrative synergies over time of approximately $160.0 million annually. By reducing expenses, and achieving the operational benefits noted above, we believe that the combined entity will move to profitability more quickly than XO would have had we not entered into the Allegiance asset acquisition.

Our acquisition of substantially all of the assets of Allegiance, although approved by the U.S. Bankruptcy Court, remains contingent upon the fulfillment of a variety of covenants contained in the definitive documentation pursuant to which we anticipate acquiring the Allegiance assets. Such contingencies include, without limitation, our obtaining regulatory clearances, such as Hart-Scott-Rodino and approval of the Federal Communication Commission, or FCC, and state public utility commissions. While we believe the approvals will be forthcoming, there can be no assurance that we will obtain the governmental approvals and clearances required to consummate our acquisition of the Allegiance assets.

Services

We provide business customers with a comprehensive array of data and voice telecommunications services, which include voice, Internet access, private data networking and hosting services. We have designed these telecommunications services to meet the needs of all sizes of commercial business customers, from small and medium businesses to multi-location businesses, large enterprises, as well as carrier and wholesale customers.

Voice Services

Local and Long Distance Voice Services

We offer a variety of voice applications and services as an alternative to comparable local services from the Incumbent Local Exchange Carriers, or ILECs. These voice services include:

- local standard dial tone, including touch-tone dialing, 911 access and operator assisted calling;
- local multi-trunk dial tone services, including direct inward dialing, and direct outward dialing;
- long distance services, including 1, toll free, calling card and operator services;
- voice messaging with personalized greetings, send, transfer, reply and remote retrieval capabilities;
- conferencing services, including voice and web conferencing services; and
- directory listings and assistance.

In each of our markets, we have negotiated and entered into interconnection agreements with the ILEC and certain independent carriers, and implemented permanent local number portability, which allows customers to retain their telephone numbers when changing telephone service providers.

Hosted Interactive Voice Response

We develop and manage hosted interactive voice response, or IVR, systems for customers that enable end users to order products and services, collect and receive information, seek assistance, facilitate bill payments, and a host of other capabilities over the telephone. Our hosted IVR capabilities utilize a wide range of technologies, from standard touch-tone/push-button dialing to natural language speech recognition and extensible markup language, or XML, and VoiceXML technologies, which are sophisticated systems that enable persons to access Web-based information over the telephone. We customize for our clients' particular needs telephony-based software applications and technologies developed by third parties to create IVR systems. We integrate these IVR systems with our clients' other business systems, such as information databases and customer relationship management systems. We host and maintain the IVR systems in data centers and deploy them to clients across a network, thereby alleviating the need for our clients to purchase, own, install, or maintain these applications. Clients pay for the use of these customized solutions through a combination of "upfront" payments for development and recurring fees based on transaction volume. We also host and manage personal identification number, or PIN, management systems for customers, which consist of primarily pre-paid calling card systems, including providing transaction processing services relating to prepaid calling card services provided by other telecommunications carriers.

Data Services

Internet Access

Our Internet access offerings include dedicated access services targeted at businesses that desire single or multipoint high-speed, dedicated connections to the Internet. Our Dedicated Internet Access service provides service guarantees for internet speeds ranging from 56 kilobits per second, or kbps, to 1 Gigabit per second, or Gbps. Our digital subscriber line, or DSL, service also includes a wide range of dedicated access speeds for Small and Medium Business, or SMBs. We are a tier-1 Internet backbone provider in the U.S., with over 200 public and private peering arrangements with other Internet backbones.

Private Data Networking

We provide dedicated transmission capacity on our networks to customers that desire high-bandwidth links between locations. We offer special access and point-to-point circuits to long distance carriers and other high volume customers, which are used as both primary and back-up circuits. In addition, fiber optic technology that enables signals to be transmitted at different wavelengths on a single fiber allows us to lease one or more dedicated wavelengths to customers that desire high-bandwidth links between locations. We currently offer these services with connections of up to 9.6 gigabits per second, a transmission rate that is described in our industry as OC-192. This service supports a variety of transmission protocols, including Asynchronous Transfer Mode or ATM, Frame Relay and Synchronous Optical Network, or SONET.

Our virtual private network, or VPN, services enable customers to deploy tailored, Internet Protocol-based mission-critical business applications for secure internal enterprise, business-to-business and business-to-customer data communications among geographically dispersed locations, while also affording high-speed access to the Internet. VPN services also provide secure access for remote users, such as traveling employees and employees working from home or a remote location, which is not possible using private line and frame relay services. We also offer managed firewall services.

Finally, we offer a suite of Ethernet services, including Gigabit Ethernet, or GigE, in most of our U.S. markets, as well as intercity Ethernet services between our markets. Our Ethernet services are designed to provide high-speed, high-capacity connections between customers' local area networks, or LANs, within and between metropolitan areas, while eliminating the need for ongoing configuration, management and acquisition of equipment by the customer. These services are designed to provide private networking data speeds ranging from 10 or 100 megabits per second to one gigabit per second connections, to simplify customers' network connections, and to significantly reduce their costs.

Hosting Services

We offer a range of applications hosting services that can manage a customer's web-based infrastructure and operational needs, allowing customers to focus on their web-based content. In addition, we provide server management tools and services to manage customers' larger computers (which are known as servers) for them.

To provide this service, we have equipped our data centers and have configured the central offices of our network backbone with electrical and environmental controls and 24-hour maintenance and technical support, to provide an attractive location for our customers to locate their servers or from which they can run important applications on servers that we maintain.

Our hosting services include:

- **Web Hosting:** support for customers' websites, including design, maintenance and telecommunications services;
- **Server Collocation:** collocation of customers' servers in our data centers; and
- **Application Hosting:** running our customers' enterprise-wide applications at our data centers and distributing them as needed over our network or servers to ensure uniformity, reduce costs and implement upgrades on a continuous and immediate basis.

As part of some of our XOptions integrated packages of telecommunications services, we offer web hosting with Microsoft's bCentral web-based tools and applications, which enables customers to conduct targeted email marketing, register their web site with hundreds of Internet search engines and directories, build catalogues and sell products over the web, and coordinate meetings and appointments online. We also offer a suite of hosting outsourcing services that provides customers web-based access to email, group distribution lists, calendaring, contacts databases management and file sharing. Hosting can be "shared", in which we own the equipment and provide the underlying services, or "dedicated," in which we provide some or all of the hosting and services from our data centers using the customer's own equipment.

Integrated Voice and Data Services

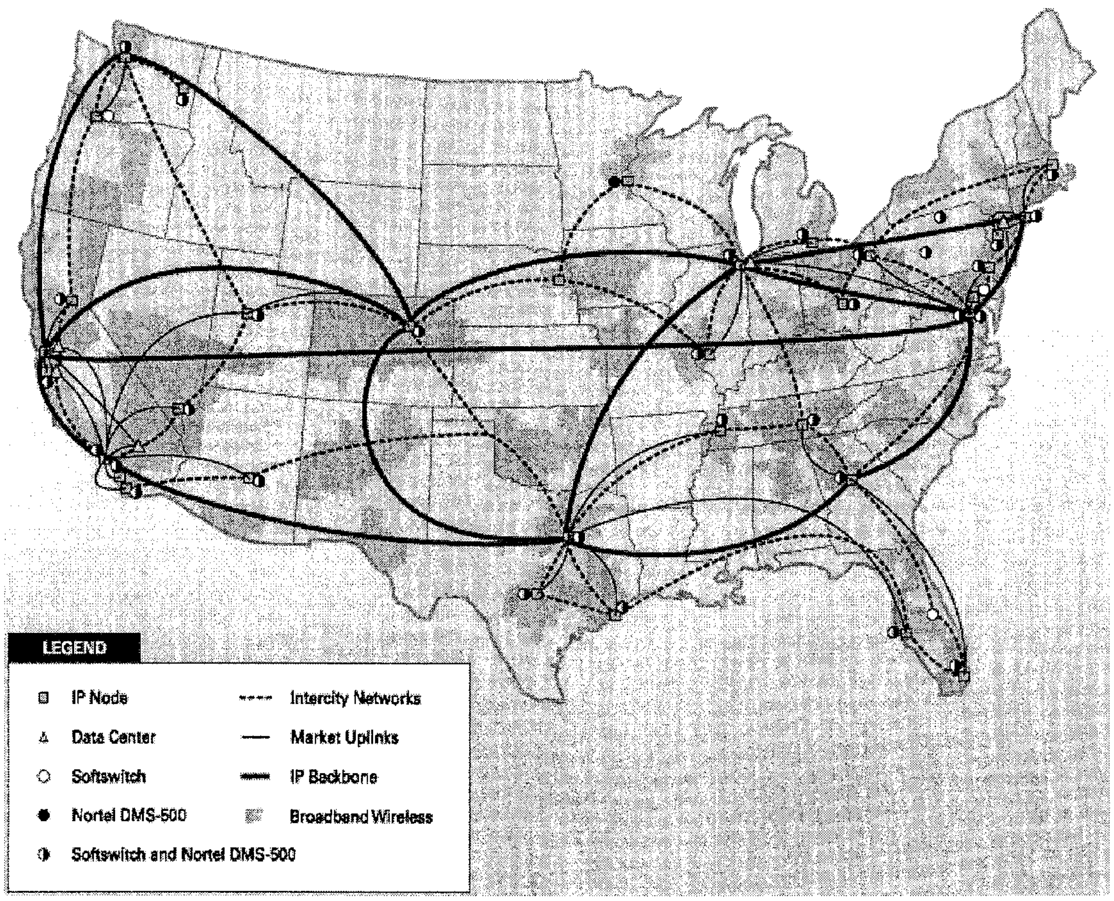
We offer bundled packages of voice and data products, known as XOptions, to small and middle-market businesses that include integrated, flat-rate packages for specified amounts of certain services, including local and long distance voice services, Internet access and web hosting services. These services include a variety of service packages designed to accommodate different sized customers with anywhere from 10 to 100 employees per location. XOptions eliminates the complexity of working with multiple service providers for installation, maintenance and billing, and also can result in significant savings over the average cost of buying these services from separate competitive voice and data providers. We also offer Integrated Access Services, which can reduce telecommunications costs by combining local voice, long distance, and dedicated Internet access on a single facility.

In 2002, we introduced a number of new XOptions packages designed to meet the needs of larger customers, specifically, those with small offices at multiple locations, those desiring to pool hosting and email accounts across multiple locations under a single account, and those that rely heavily on voice communications services. We also introduced XOptions packages that combine the benefits of XOptions' local and long distance voice, Internet access and web hosting with Microsoft's bCentral web-based tools and applications.

Our integrated services also include shared tenant services, which are telecommunications management services provided to groups of small and middle-market businesses located in the same office building. This service enables businesses too small to justify hiring their own telecommunications managers to benefit from the efficiencies, including volume discounts, normally available only to larger enterprises. We install an advanced telecommunications system throughout each building we serve, leasing space for on-site sales and service, and offer tenants products and services such as telephones, voice mail, local calling lines, discounted long distance and high-speed Internet connections, all on a single, detailed invoice.

XO's Networks

The following diagrams depict the physical components of our nationwide networks and technology. There are additional maps located on our web site at www.xo.com.



Metro Fiber Networks

The core of each of our metro fiber networks is a ring of fiber optic cable in a city's central business district that connects to our central offices. These central offices contain the switches and routers that direct data and voice traffic to their destinations, and also have the space to house the additional equipment necessary for future telecommunications services. Whenever we can, we build and own these metro fiber networks ourselves or obtain indefeasible rights to use fiber so that we can control the design and technology used to best meet our customers' needs. We operate 37 metro fiber networks serving the markets noted below:

State	Metro Fiber Network Location	Service Market
AZ	Phoenix	Phoenix*
CA	Los Angeles	Los Angeles*
CA	Orange County	Anaheim* Costa Mesa* Fullerton* Garden Grove* Huntington Beach* Inglewood* Irving* Long Beach* Orange* Santa Ana*
CA	Sacramento	Sacramento*
CA	San Diego	San Diego*
CA	San Francisco	San Francisco* Oakland* Fremont* Milpitas* Mountain View* Palo Alto* Santa Clara* Sunnyvale*
CA	San Jose	San Jose*
CO	Denver	Denver* Boulder-Longmont
DC/VA	Washington DC/ No VA	Washington, DC-MD-VA-WV*
FL	Ft Lauderdale	Ft Lauderdale*
FL	Miami	Miami* West Palm Beach-Boca Raton*
FL	Orlando	Orlando
FL	Tampa	Tampa-St. Petersburg-Clearwater*
GA	Atlanta	Atlanta* Marietta*
IL	Chicago	Chicago*
MA	Boston	Boston, MA-NH* Brockton Lawrence, MA-NH* Lowell, MA-NH* Worcester, MA-CT
MD	Baltimore	Baltimore*
MI	Detroit	Detroit*
MN	Minneapolis	Greater Minneapolis/St. Paul*
MO	St Louis	St Louis*
NJ	New Jersey	Bergen/Passaic* Middlesex-Somerset-Hunterdon Newark* Jersey City* Monmouth-Ocean Trenton
NV	Las Vegas	Las Vegas
NY	New York	Manhattan* Nassau-Suffolk*
OH	Cleveland/Akron	Cleveland-Lorain-Elyria* Akron Canton-Massillon
OH	Columbus	Columbus
OR	Portland	Portland-Vancouver, OR-WA
PA/DE	Central PA	Allentown-Bethlehem-Easton* Harrisburg-Lebanon-Carlisle Lancaster Reading Scranton-Wilkes-Barre-Hazleton York Wilmington-Newark, DE-MD Dover*
PA	Philadelphia	Philadelphia, PA-NJ*
TN	Memphis	Memphis, TN-AR-MS
TN	Nashville	Nashville
TX	Austin	Austin-San Marco*
TX	Dallas/Ft Worth	Dallas*
TX	Houston	Fort Worth-Arlington* Houston*
TX	San Antonio	San Antonio*
UT	Salt Lake City	Salt Lake City-Ogden Orem/Provo
WA	Seattle	Seattle-Bellevue-Everett*
WA	Spokane	Spokane Lewiston Clarkston Coeur d'Alene

* Indicates markets with Allegiance service presence. In addition, Allegiance has a service presence in Pittsburgh, PA and White Plains, NY.

We built our high capacity metro fiber networks using a backbone density typically ranging between 72 and 432 strands of fiber optic cable. Fiber optic cables have the capacity, or bandwidth, to carry tens of thousands of times the amount of traffic as traditionally-configured copper wire. We believe that installing high-count fiber strands will allow us to offer a higher volume of broadband and voice services without incurring significant additional construction costs. To enhance our ability to economically connect customers to our networks and services, we design our networks to serve both core downtown areas and other metropolitan and suburban areas where business development supports the capital required for the network construction.

Intercity Network

We provide intercity transport primarily through five year leases of wavelength capacity from Level 3 on routes linking our metro fiber networks to one another and onto which we have deployed transmission and routing equipment to create a single, end-to-end network. The first of these leases will expire in 2006. We expect to either renew the leases for wavelengths or to light our intercity fiber network discussed below based on the most cost effective approach. We have designed and installed much of the equipment we use to route traffic and control our intercity wavelengths so that we can easily transfer voice and data traffic from leased wavelength capacity onto our intercity fiber network as portions of that network are lit. By using our own transmission and routing equipment, we maximize the capacity and enhance the performance of the network as needed to meet our customers' current and future broadband data and other telecommunications needs.

Using Level 3 leased wavelength capacity and our own routers and transport equipment, we also operate an OC-192 capacity Internet backbone, onto which a substantial amount of our Internet-related services and customer traffic runs. This backbone provides our customers with improved network redundancy, security and performance, and enables us to offer customers services that take advantage of future Internet Protocol technologies.

In addition to our Level 3 leased wavelength capacity, we have intercity fiber network assets primarily consisting of an exclusive interest in 18 fibers in a shared, filled conduit in the Level 3 North American network, substantially all of which are unlit. These fibers are part of a fiber network that traverses over 16,000 miles and connects more than 60 cities in the United States and Canada, including most of the major metropolitan markets served by our metro networks.

To conserve capital, we delayed "lighting" much of our intercity fiber network. In order to light a segment of our intercity fiber network, we would install optical network equipment at our facilities that would allow for the transmission and routing of network traffic over that fiber segment. In the aggregate, the capital expenditures that would be required to light our entire intercity network would be approximately $45 million. Given the level of traffic in relationship to capacity and the current availability of intercity wavelength capacity that is available to us at cost-efficient lease rates, to date it has generally been more cost-effective to lease the required intercity wavelength capacity rather than light our own intercity network.

However, along specific segments of our intercity network where the demand for telecommunications capacity justifies the required capital expenditures, we have proceeded with lighting those specific segments. Due to the need for additional, cost efficient capacity along the segment that runs from Los Angeles to San Diego, we lit this segment in June 2003, and we lit the Denver to Salt Lake City segment in November 2003. Additionally, we previously lit fiber acquired from Metromedia Fiber Network, Inc. that runs from New York to Washington, D.C. to provide an additional route to the lit intercity fiber network along that segment and we have also lit fiber in Texas. As discussed above, as leases for segments of wavelength capacity expire, we will either renew the leases for wavelengths or light our intercity fiber segment based on the most cost effective approach.

In August 2002, we entered into a Master Agreement with Level 3 Communications, Inc., which amends various agreements related to our acquisition of fiber networks in the United States from Level 3 and the recurring maintenance charges relating to those networks. Beginning on January 1, 2003 and continuing through the remaining term of the initial agreement ending 2018, Level 3 has reduced the operating and maintenance fees as well as fiber relocation charges from approximately $17.0 million annually to a fixed rate of $5.0 million annually. In exchange for this reduction and certain other concessions, we surrendered our indefeasible right to use an empty conduit and our indefeasible right to use six of the 24 fibers previously acquired from Level 3 and recorded a one-time charge of approximately $477.3 million in connection therewith. We believe that the 18 fibers that we retained from Level 3 in connection with the execution of the Master Agreement will be sufficient capacity to expand our business.

Connecting Customers to Our Networks

We connect our customers directly to our networks when it is economical and technologically feasible to do so. We connect customers to our networks by using fiber optic cable and, in limited circumstances, broadband wireless spectrum. We believe that by deploying direct connections to our customers, rather than connecting through the ILECs' facilities, we will reduce our costs and be better positioned to meet our customers' telecommunications requirements and to more rapidly deploy our service.

In most cases, we are required to lease facilities from an ILEC to connect a customer to our network. By building our metro fiber networks in central business districts, in many cases we have minimized the distance from our network to a potential customer. By reducing the distance between our customers and our network, we have minimized the costs associated with the facilities we lease from the ILECs because the cost of those facilities is generally based, on the distance of the leased connection.

Fiber Optics. In cases where the anticipated revenues justify the construction cost, we will install a new fiber optic extension from our network to the customer's premises. Whether it is economical to construct a fiber optic extension depends, among other things, on:

- the existing and potential revenue base located in the building in question;
- the building location relative to our network and our ability to access the communications equipment in that building, and
- local permit requirements and construction costs.

Even if we initially determine that it is not economical to construct a fiber connection to a building, we will continually reexamine the costs and benefits of a fiber connection and may, at a later date, determine that construction of one is justified.

Broadband Wireless Spectrum. In cases where construction of a fiber optic connection is not practical or economical, in limited cases we have deployed a high-bandwidth wireless connection between an antenna on the roof of the customer's premises and an antenna attached to our metro fiber network. In those limited cases, we and/or our customers must secure roof and other building access rights, including access to conduits and wiring from the owners of each building or other structure on which we propose to install our equipment, and may need to obtain construction, zoning, franchise or other governmental permits.

DSL Technology. We have also deployed DSL technology to meet the high-bandwidth needs of many customers located less than three miles from the ILEC's central office and whose customer connection remains over copper wire. DSL technology reduces the bottleneck in the transport of information, particularly for data services, by increasing the data carrying capacity of copper telephone lines. We believe that, for many small and middle-market businesses within the geographic areas that can be served by DSL technology, existing copper connections using DSL technology from customer buildings to our metro fiber networks offers a lower cost alternative for high-quality broadband services than fiber or broadband wireless connections.

We offer DSL services in numerous markets in the U.S., mainly through wholesale arrangements with the ILECs and other DSL service providers. We have introduced our own DSL equipment and services at many collocation sites, including central offices of the ILECs that serve a significant number of business customers.

Network Technology

Overview

The wires, cables and spectrum that comprise the physical layer of our networks can support a variety of communications technologies. We seek to offer customers a set of technology options that can support services that meet their changing needs and introduce new technologies as necessary. Specifically, we believe that a service platform based on Internet Protocol, or IP, will provide us with significant future opportunities, because it will enable data, voice and video to be carried inexpensively over our end-to-end, facilities-based network. Consequently, we have supplemented our current data and voice switching technology with IP equipment.

Over the past few years, both optical and IP-based networking technologies have undergone rapid innovation. These technological developments enable us to offer our customers numerous high-speed data services. Many of these innovations have the effect of increasing the efficiency of the physical components of our network by increasing the effective capacity of networks for these types of applications. In the future, we expect that IP-based technology will become the preferred technology for voice calls and facsimile transmission as well. We plan to remain flexible in our use of technology, so that, as underlying telecommunications technology changes, we will have the ability to take advantage of and implement new technologies that best meet our network requirements and customers' needs.

Fiber Optic Technology

To enhance the capacity of our metro fiber networks, we are incorporating dense wavelength division multiplexing technology, which makes it possible to simultaneously transmit data at more than one wavelength. This capability allows the transmission of multiple signals through the same fiber at different wavelengths. When utilized with the optical fiber deployed in many of our metro fiber networks and in our intercity network, this technology can significantly increase the capacity of those metro fiber networks.

Switching Technology

There are two commonly used switching technologies currently deployed in most telecommunications networks: circuit switched-based systems and packet switched-based systems. Circuit switch-based systems are currently used on a majority of telecommunications networks. Circuit switch-based systems establish a dedicated channel for each telecommunication signal (such as a telephone call for voice or fax), maintain the channel for the duration of the call, and disconnect the channel at the conclusion of the call.

Packet switch-based telecommunications systems, which format the information to be transmitted into a series of shorter digital messages called "packets," are the preferred means of data transmission. Each packet consists of a portion of the complete message plus the addressing information to identify the destination and return address. A key feature that distinguishes Internet architecture from the public telephone network is that on the packet-switched Internet, a single dedicated channel between telecommunication points is not required.

Packet switch-based systems offer several advantages over circuit switch-based systems, particularly the ability to commingle packets from several telecommunications sources together simultaneously onto a single channel. For most telecommunications, particularly those with bursts of information followed by periods of "silence," the ability to commingle packets provides for superior network utilization and efficiency, resulting in more information being transmitted through a given telecommunication channel.

IP technology, an open protocol that allows unrelated computer networks to exchange data, is the technological basis of the Internet. The Internet's explosive growth in recent years has focused intensive efforts worldwide on developing IP-based networks and applications. In contrast to protocols like ATM, which was the product of elaborate negotiations between the world's monopoly telephone companies, IP is an open standard, subject to continuous improvement.

We believe that a form of IP-based switching will eventually replace both ATM and circuit switched technologies, and will be the foundation of integrated networks that treat all transmissions — including voice, fax and video — simply as forms of data transmission. Although not always the case, voice over IP, or VoIP, technology now incorporates the quality of service necessary for commercial deployments, but the pricing of equipment that must be installed at customer locations in order to implement VoIP applications is not yet cost-effective for widespread application. We expect that, over time, improved technology and the manufacture of sufficient volumes of equipment will make customer adoption of VoIP applications more cost-effective.

We have constructed IP points of presence in all of our major markets using high-capacity IP routers, through which we offer Internet-related services. We currently connect these points of presence with our intercity fiber network, which serves as our OC-192 IP backbone.

We have deployed a number of newly-developed packet-based switching technologies, including soft-switch, optical and Ethernet switching technologies. The soft-switch is a distributed computer system that performs the same functions as a circuit switch. It can route and switch information at an extremely fast rate. Initially, we will use soft-switch technology to complement and relieve traffic from our circuit switches. We have deployed optical switching, routing and transmission equipment on our intercity network to create an all-optical network. This technology is designed to make significant amounts of bandwidth available to our customers. It also is designed to enable us to more effectively and efficiently manage our customers' transmissions and to enhance our deployment of dense wavelength division multiplexing technology. Optical switching will support all transmission protocols, including IP, ATM, and frame relay. We also are deploying Ethernet switching technology to support and expand our Ethernet services.

Broadband Wireless Technology

We hold 91 local multipoint distribution service or LMDS licenses and ten 39 GHz licenses. There are additional holders in some of the cities where we hold licenses. The following tables shows (i) the license number, (ii) the metropolitan areas and frequency band for each area covered by the license, (iii) the estimated population for each area, (iv) the amount of spectrum for each area, and (v) the expiration date for each license. This makes us the licensee of the largest US footprint of fixed wireless spectrum.

License Number	City	State	Population	A Band	B Band	39 GHz Chanls	License Renewal
WPOL286	New York (PMSA of 5 boroughs & 3 counties)	NY	8,546,846	A3			2/1/2006
WPLM417	Atlanta	GA	3,197,171		B		6/17/2008
WPLM412	Austin	TX	899,361		B		6/17/2008
WPLM416	Baltimore	MD	2,430,563		B		6/17/2008
WPLM430	Birmingham	AL	1,200,336	A			6/17/2008
WPLM413	Boston	MA	4,133,895		B		6/17/2008
WPLM418	Chattanooga	TN	510,860	A			6/17/2008
WPLM405	Chicago	IL	8,182,076		B		6/17/2008
WPLM424	Cincinnati	OH	1,990,451		B		6/17/2008
WPLM422	Cleveland-Akron	OH	2,894,133		B		6/17/2008
WPLM410	Columbia	SC	568,754	A			6/17/2008
WPLM438	Columbus	OH	1,477,891		B		6/17/2008
WPON926	Denver	CO	2,073,952	A1(part)			6/17/2008
WPLM408	Detroit	MI	4,705,164		B		6/17/2008
WPLM398	Hartford	CT	1,123,678		B		6/17/2008
WPLM411	Hickory-Lenoir-Morganton	NC	292,409	A			6/17/2008
WPLM431	Huntsville	AL	439,832	A			6/17/2008
WPLM435	Indianapolis	IN	1,321,911		B		6/17/2008
WPLM436	Kansas City	MO	1,839,569		B		6/17/2008
WPLM434	Klamath Falls	OR	74,566		B		6/17/2008
WPLM420	Lakeland-Winterhaven	FL	405,382		B		6/17/2008

License Number	City	State	Population	A Band	B Band	39 GHz Chanls	License Renewal
WPLM429	Lexington	KY	816,101	A			6/17/2008
WPLM401	Los Angeles*	CA	14,549,810	A			6/17/2008
WPLM428	Louisville	KY	1,352,955	A			6/17/2008
WPLM423	Mansfield	OH	221,514		B		6/17/2008
WPLM433	Medford-Grants Pass	OR	209,038		B		6/17/2008
WPOH970	Milwaukee	WI	1,751,525	A			6/17/2008
WPLM419	Minneapolis-St. Paul	MN	2,840,561	A			6/17/2008
WPOH945	New Haven-Waterbury-Meriden	CT	978,311		B		6/17/2008
WPLM400	New London-Norwich	CT	357,482		B		6/17/2008
WPLM397	New York (whole BTA)	NY	18,050,615		B		6/17/2008
WPLM421	Ocala	FL	194,833		B		6/17/2008
WPLM432	Portland	OR	1,690,930	A			6/17/2008
WPOH956	Providence-Pawtucket, New Bedford-Fall River	RI,MA	1,509,789	A			6/17/2008
WPLM437	Rochester	NY	1,118,963		B		6/17/2008
WPLM407	Sacramento	CA	1,656,581	A			6/17/2008
WPLM402	San Diego	CA	2,498,016		B		6/17/2008
WPLM406	San Francisco-Oakland-San Jose	CA	6,420,984		B		6/17/2008
WPLM404	San Luis Obispo	CA	217,162	A			6/17/2008
WPLM403	Santa Barbara-Santa Maria	CA	369,608	A			6/17/2008
WPLM427	Seattle-Tacoma	WA	2,708,949	A			6/17/2008
WPLM425	St. Louis	MO	2,742,114		B		6/17/2008
WPLM409	Toledo	OH	782,184		B		6/17/2008
WPLM415	Washington	DC	4,118,628		B		6/17/2008
WPOH677	Albuquerque	NM	688,612	A			9/1/2008
WPOH679	El Paso	TX	649,860	A			9/1/2008
WPOH676	Tucson	AZ	666,880	A			9/1/2008
WPOH683	Lawton-Duncan	OK	177,830	A			9/1/2008
WPOH682	Oklahoma City	OK	1,305,472	A			9/1/2008
WPOH684	Omaha	NE	905,991	A			9/1/2008
WPOH676	Tulsa	OK	836,559	A			9/1/2008
WPHOH944	Albany-Schenectady	NY	1,028,615	A			10/6/2008
WPOH963	Atlanta	GA	3,197,171	A			10/6/2008
WPOH954	Austin	TX	899,361	A			10/6/2008
WPOH962	Baltimore	MD	2,430,563	A			10/6/2008
WPOH955	Boston	MA	4,133,895	A			10/6/2008
WPOH955	Buffalo-Niagara Falls	NY	1,231,795	A			10/6/2008
WPOH950	Charlotte-Gastonia	NC	1,671,037	A			10/6/2008
WPOH948	Chicago	IL	8,182,076	A			10/6/2008
WPOH953	Dallas	TX	4,329,924	A			10/6/2008
WPOH975	Des Moines	IA	728,830	A			10/6/2008
WPOH949	Detroit	MI	4,705,164	A			10/6/2008
WPOH952	Greenville-Spartanburg	NC	788,212	A			10/6/2008
WPOH943	Hartford	CT	1,123,678	A			10/6/2008
WPOH966	Houston	TX	4,054,253	A			10/6/2008
WPOH974	Indianapolis	IN	1,321,911	A			10/6/2008
WPOH979	Jacksonville	FL	1,114,847	A			10/6/2008
WPOH981	Knoxville	TN	948,055	A			10/6/2008
WPOH947	Los Angeles	CA	14,549,810		B		10/6/2008
WPOH959	Manchester-Nashua-Concord	NH	540,704	A			10/6/2008
WPOH973	Memphis	TN	1,396,390	A			10/6/2008
WPOH967	Miami-Ft. Lauderdale	FL	3,270,606	A			10/6/2008
WPLM426	Milwaukee	WI	1,751,525		B		10/6/2008
WPOH964	Minneapolis-St. Paul	MN	2,840.561		B		10/6/2008
WPOH980	Nashville	TN	1,429,309	A			10/6/2008

License Number	City	State	Population	A Band	B Band	39 GHz Chanls	License Renewal
WPLM399	New Haven-Waterbury-Meriden	CT	978,311	A			10/6/2008
WPOH942	New York (unencumbered by PMSA) Philadelphia, Wilmington (DE), Trenton	NY	9,503,769	A			10/6/2008
WPOH960	(NJ)	PA	5,899,345	A			10/6/2008
WPOH971	Pittsburgh Providence-Pawtucket, New Bedford-Fall	PA	2,507,839	A			10/6/2008
WPLM414	River	RI,MA	1,509,789		B		10/6/2008
WPOH951	Raleigh-Durham	NC	1,089,423	A			10/6/2008
WPOH972	Richmond-Petersburg	VA	1,090,869	A			10/6/2008
WPOH978	Rochester	NY	1,118,963	A			10/6/2008
WPOH976	San Antonio	TX	1,530,954	A			10/6/2008
WPOH958	Springfield-Holyoke	MA	672,970	A			10/6/2008
WPOH969	St. Louis	MO	2,742,114	A			10/6/2008
WPOH946	Syracuse	NY	791,140	A			10/6/2008
WPOH965	Tampa-St. Petersburg-Clearwater	FL	2,249,405	A			10/6/2008
WPOH961	Washington	DC	4,118,628	A			10/6/2008
WPOH968	West Palm Beach-Boca Raton	FL	893,145	A			10/6/2008
WPOH957	Worcester-Fitchburg-Leominster	MA	709,705	A			10/6/2008
WPQT938	Denver-Boulder-Greeley	CO	2,073,952			B	10/18/2010
WPQT942	Las Vegas	NV	857,856			E	10/18/2010
WPQT946	Las Vegas	NV	857,856			G	10/18/2010
WPQT939	San Diego	CA	2,498,016			B	10/18/2010
WPQT944	San Diego	CA	2,498,016			F	10/18/2010
WPQT947	San Diego	CA	2,498,016			N	10/18/2010
WPQT940	San Francisco	CA	6,420,984			D	10/18/2010
WPQT945	San Francisco	CA	6,420,984			F	10/18/2010
WPQT941	Toledo	OH	782,184			E	10/18/2010
WPQT943	Toledo	OH	782,184			F	10/18/2010

Legend

A	27,500 to 28,350 MHz, 29,100 to 29,250 GHz, 31,075 to 31,225 GHz 1,150 MHz
A1	27,500 to 28,350 MHz 850 MHz
A3	31,075 to 31,225 GHz 150 MHz
B	31,000 to 31,075 MHz, 31.225 to 31,300 MHz 150 MHz
39 GHz B	38,650 to 38,700 MHz, 39,350 to 39,400 100 MHz
39 GHz E	38,800 to 38,850 MHz, 39,500 to 39,550 100 MHz
39 GHz G	38,900 to 38,950 MHz, 39,600 to 39,650 100 MHz
39 GHz F	38,850 to 38,900 MHz, 39,550 to 39,600 100 MHz
39 GHz N	39,250 to 39,300 MHz, 39,950 to 40,000 100 MHz
39 GHz D	38,750 to 38,800 MHz, 39,450 to 39,500 100 MHz

The higher the frequency, the higher the attenuation (loss). For the same amount of transmission power, a lower frequency signal will propagate farther.

The spectrum under the licenses we hold is not suitable for mobile telephones, but can transmit voice, data or video signals from one fixed antenna to one or many others. As the word "local" in the local multipoint distribution service name implies, the radio links provided using LMDS frequencies are of limited distance, typically five miles or less, due to the degradation of these high-frequency signals over greater distances. This also is true of the 39 GHz spectrum.

A wireless connection typically consists of paired antennas placed at a distance of up to 5 miles from one another with a direct, unobstructed line of sight. The antennas are typically installed on rooftops, towers or windows. This technology works by connecting the end user through fixed wireless access to points of presence on our metro fiber network, thus eliminating the need for the RBOC's last mile of infrastructure. This third generation fixed wireless broadband access, in conjunction with our intercity and metro fiber network, allows us to offer a wide range of metro, national and global connectivity solutions.

There are additional holders in some of the cities where we hold licenses. There are also competitors who are licensed broadband fixed wireless operators in the 39 GHz spectrum bands. Examples include First Avenue Networks and AT&T Business Services. There are existing users of the 39 GHz spectrum that may require XO as a new user of the spectrum to coordinate its use to avoid interference with an existing user. We do not believe that the coordination process will significantly limit our ability to make use of the spectrum.

The term of the licenses for our broadband wireless spectrum generally is ten years. Although the licenses are renewable for an additional ten year term, renewal is conditioned on our ability to satisfy utilization requirements established by the FCC. During 2003 we had successful trials in our San Diego and Irvine, California markets and deployed services at approximately 20 customers. We continue to evaluate recent improvements in the price and performance of fixed wireless equipment, and have plans to meet the FCC's "substantial service" test before the licenses are due for renewal proceedings. In the event that we do not meet the FCC's substantial service test at the end of the license expiration date, we may request an extension of time or waiver of license forfeiture from the FCC.

Sales, Network Services and Customer Care

Sales Overview

Our sales organization includes a direct field sales force and indirect sales channels. Our direct sales force includes two sales organizations, one that addresses the needs of commercial customers and one that services carrier accounts. Our commercial sales organization focuses on all retail customers, growing businesses within a market, developing multi-market accounts and targeting national accounts. Our carrier sales organization focuses solely on servicing telecommunications providers who, in combination with other capabilities, provide telecommunications services under their own brand.

Our market research indicates that commercial customers prefer a single source for all of their telecommunications requirements, including products, billing, installation, maintenance, and customer service. By offering these customers our local, long distance or data services individually or through our XOptions packages, which combine local and long distance voice services, Internet access and web hosting services, we believe we provide our customers a level of convenience that generally is unavailable in the telecommunications marketplace.

We market and sell our products to other telecommunications providers through our carrier services organization. These customers benefit from our national network, our data service capabilities, our broad range of services and our cost effective solution design.

Direct Sales Force

We have established a highly motivated and experienced direct sales forces. Our strategy is to design the structure of our sales efforts so that our sales personnel are able to develop a direct and personal relationship with our customers. We seek to recruit salespeople with strong sales and telecommunications backgrounds, including salespeople from long distance companies, telecommunications equipment manufacturers, network systems integrators and the ILECs. Our salespeople are offered incentives through a commission structure that generally targets 40% to 50% of a salesperson's total compensation to be based on performance. Our direct sales and sales support organization consisted of approximately 1,700 employees at December 31, 2003, up from approximately 1,100 employees at December 31, 2002. As part of the performance review process and to reduce expenses, the sales organization declined to approximately 1,200 in March 2004. We will continue to evaluate sales performance and revenue growth in the most cost effective manner.

Indirect Sales Channels

We have complemented our direct sales force by developing an indirect sales channels to distribute the increasing number of products and services available to our customer base. These channels include numerous third party sales agents. We currently have distribution arrangements with a number of national, regional and local agents and agency firms, whose representatives market a broad range of XO services. As of December 31, 2003, we had staff of approximately 60 employees who manage our agent relationships and more than 700 indirect sales agents in markets throughout the United States. During the fourth quarter of 2003, approximately 20% of new sales were generated by indirect agents.

Network Services

Our network services organization consists of 2,100 employees whose main objective is to deliver superior service and to enhance the customers' experience. Network service employees are located in all of our markets. Their main objectives include the design, deployment, maintenance and when necessary, repair of our network assets. In addition, they are responsible for installing customer premise equipment and activating new customers as well as maintaining and when necessary, repairing any service outages our customers might experience. We maintain a very competitive median repair time.

Customer Care

Once a customer's services have been installed, our customer care operations support customer retention and satisfaction. Our goal is to provide customers with a customer care group that has the ability and resources to respond to and resolve customer questions and issues as they arise. In 2003, although we conducted much of our customer care operations from three call centers, we also provided locally-based care for many large customers. Because we believe that a more centralized care structure not only takes advantage of economies of scale, but also enables us to provide better customer service, we closed one of our care facilities in 2003. The size of our customer care organization has remained constant from December 31, 2002 to December 31, 2003, with approximately 700 employees.

Regulatory Overview

Overview

The Telecommunications Act of 1996, or the "Telecom Act", which substantially revised the Communications Act of 1934, established the regulatory framework for the introduction of competition for local telecommunications services throughout the United States by new competitive independent entrants such as us. Prior to the passage of the Telecom Act, states typically granted an exclusive franchise in each local service area to a single dominant carrier — often a former subsidiary of AT&T known as an RBOC — which owned the entire local exchange network and operated a virtual monopoly in the provision of most local exchange services in most locations in the United States. The RBOCs, following some recent consolidation, now consist of the following companies: BellSouth, Verizon, Qwest Communications and SBC Communications.

Among other things, the Telecom Act preempts state and local governments from prohibiting any entity from providing telecommunications service, which has the effect of eliminating prohibitions on entry that existed in almost half of the states at the time the Telecom Act was enacted. At the same time, the Telecom Act preserved state and local jurisdiction over many aspects of local telephone service and, as a result, we are subject to varying degrees of federal, state and local regulation. Consequently, federal, state, and local regulation, and other legislative and judicial actions relating to the telecommunications industry could significantly affect our business.

We believe that the Telecom Act provided the opportunity to accelerate the development of competition at the local level by, among other things, requiring the incumbent carriers to cooperate with competitors' entry into the local exchange market. We have developed our business and designed and constructed our networks to take advantage of the features of the Telecom Act that require cooperation from the incumbent carriers, and believe that the continued viability of the pro-competitive statutory provisions is critical to the success of the competitive framework contemplated by the Telecom Act.

Although the Telecom Act and the related rules governing competition issued by the FCC, as well as pro-competitive policies already developed by state regulatory commissions, have enabled new entrants like us to capture a portion of the incumbent carriers' market share of local services, there have been numerous attempts to limit or eliminate the basic framework for competition in the local exchange services market through a combination of federal legislation, adoption of new rules by the FCC, and RBOC challenges to existing and proposed regulations. We expect these efforts to limit the benefits of the Telecom Act to continue. Successful implementation of our business plan is predicated on the assumption that the basic competitive framework will remain in place.

Federal Regulation

The FCC exercises jurisdiction over our telecommunications facilities and services. We have authority from the FCC for the installation, acquisition and operation of our wireline network facilities to provide facilities-based domestic interstate and international services. In addition, we have obtained FCC authorizations for the operation of our LMDS and 39 GHz broadband wireless facilities. Unlike incumbent carriers, we are not currently subject to price cap or rate of return regulation, which leaves us free to set our own pricing policies for end user services subject only to the general federal guidelines that our charges for interstate and international services be just, reasonable, and non-discriminatory. The FCC allows us to file interstate tariffs for interstate access services (rates charged by carriers for access to their networks). The FCC, however, required that, with only minor exception, we withdraw our tariffs for interstate domestic long distance services and international long distance services. We, however, are still required to make the terms, conditions and rates of the detariffed services available to the public on our Company web page, and such terms, conditions, and rates are located at http://www.xo.com/legal/.

The following is a summary of the interconnection and other rights granted by the Telecom Act that are important for effective local service competition and our belief as to the effect of the requirements, if properly implemented:

- Interconnection with the networks of incumbents and other carriers, which permits our customers to exchange traffic with customers connected to other networks;
- Local loop and transport unbundling, which allows us to selectively gain access to incumbent carriers' facilities and wires that connect the incumbent carriers' central offices and/or customer premises, thereby enabling us to serve customers not directly connected to our networks;
- Reciprocal compensation, which mandates arrangements for local traffic exchange between us and both incumbent and competitive carriers and compensation for terminating local traffic originating on other carriers' networks, thereby improving our margins for local service;
- Number portability, which allows customers to change local carriers without changing telephone numbers, thereby removing a significant barrier for a potential customer to switch to our local voice services;
- Access to phone numbers, which mandates assignment of new telephone numbers to our customers, thereby enabling us to provide telephone numbers to new customers on the same basis as incumbent carriers; and
- Collocation of telecommunications equipment in incumbent carrier central offices, which enables us to have direct access to unbundled loops and other network elements and facilitates for efficient integration with our switching and other network facilities.

In January 1999, the U.S. Supreme Court, in a decision that was generally favorable to competitive telephone companies such as us, upheld key provisions of the FCC rules implementing the Telecom Act. In finding that the FCC has general jurisdiction to implement the Telecom Act's local competition provisions, the Court confirmed the FCC's role in establishing national telecommunications policy, and thereby created greater certainty regarding the rules governing local service competition on a going forward basis.

Although the rights established in the Telecom Act are a necessary prerequisite to the introduction of full local competition, they must be properly implemented and enforced to permit competitive telephone companies like us to compete effectively with the incumbent carriers. Discussed below are several FCC and court proceedings relating to the application of certain FCC rules and policies that are significant to and directly impact our operations as well as the nature and scope of industry competition.

Unbundling of Incumbent Network Elements

In the January 1999 Supreme Court decision discussed above, the Court affirmed the FCC's interpretation of matters related to unbundling of incumbent carriers' network elements. It held that the FCC correctly interpreted the meaning of the term "network element", which defines the parts of an incumbent carrier's operations that may be subject to the "unbundling" requirement of the Telecom Act. The Court, however, also held that the FCC did not correctly determine which network elements must be unbundled and made available to competitive telephone companies such as us. In November 1999, the FCC released its "UNE (unbundled network element) Remand Order", which addressed the deficiencies in the FCC's original ruling cited by the Court. The order generally was viewed as favorable to us and other competitive carriers because it ensured that incumbent carriers would be required to continue to make available those network elements, including unbundled loops, that are crucial to our ability to provide local and other services. The UNE Remand Order subsequently was appealed by the incumbent carriers.

On May 24, 2002, the United States Court of Appeals for the D.C. Circuit released an opinion remanding the UNE Remand Order to the FCC for further consideration.

In response to the Court of Appeals' decision, and as part of its statutorily required periodic review of its list of unbundled elements, the FCC initiated its "Triennial Review" proceeding.

On August 21, 2003, the FCC released its Triennial Review Order ("TRO"). Under the TRO, our ability to obtain access to certain unbundled network elements and incumbent network upgrades may be curtailed or more costly in the future. Interconnection agreements that we have in place with the ILECs need to be amended to incorporate many of the TRO changes. We have started the negotiation process to complete these interconnection agreement amendments and anticipate that the agreements will be finalized during the second quarter of 2004. At this time, we cannot predict the full effect of the implementation of the TRO. Also, the TRO has delegated to the states the overall responsibility for deciding whether certain unbundled elements should remain available to competitors like us in local markets of each of the respective states. Delegation of these determinations creates the risk that some states may decide to limit or eliminate certain unbundled elements to which we have access today and that we will be faced with different sets of rules and costs if states issue inconsistent decisions.

The following Triennial Review Order matters directly impact us and many of our competitors:

- Curtailed Access to Broadband: The TRO adopted new rules that, for certain very small customers, restrict competitive carriers from leasing as unbundled elements certain upgrades that the incumbent carriers make to their networks, such as the deployment of new optical fiber or upgrades from copper to optical fiber. For example, a new fiber loop to a very small customer that replaces an existing copper loop could be exempt from unbundling, except that incumbents must continue to unbundle the pre-existing copper loop or provide a voice channel for us on the new fiber loops that is equivalent to the old copper loop. Although the imposition of any restrictions on our access to the incumbents' broadband networks is not a favorable development for us, we believe that the adverse impact is partially mitigated by the fact that incumbents are required to continue to provide us with basic access to those facilities that we currently lease from them to serve many of our customers.
- Unbundled Local Loops: The Order made a general, national finding that, with the exception of optical carrier ("OC") level loops, competitive carriers should have access to unbundled loops of the incumbent carriers. The states, however, may remove competitive carriers' access to certain

non-OC level high capacity and unlit capacity loops based on the results of specified competitive analyses. Incumbent carriers will no longer be required to provide competitive carriers with access to OC level loops. We believe that the net result of these changes will not have a significant impact on us because the access to the vast majority of unbundled loops that we use today will be preserved.

- Unbundled Dedicated Transport: The TRO has changed the definition of "dedicated transport" in such a way that competitive carriers have to purchase certain transport facilities at higher rates. The TRO maintained unbundled access to many types of transport between incumbent facilities, such as transport between incumbent central offices, but it redefines dedicated transport to eliminate the unbundling of other transport. The TRO also sets forth a test that the states must follow in considering whether certain non-OC level high capacity transport should be available in local markets within the states. The FCC also ruled that OC level transport would no longer be available as an unbundled element and that shared transport would be unavailable as an unbundled element in most business markets. We believe that it is likely that this determination will raise our costs for transport services in the future.

- Enhanced Extended Links and Co-Mingling: The TRO enhance the ability of competitive carriers like us to obtain a combination of unbundled loop and transport elements known as "enhanced extended links", provided that the underlying loop and transport elements are individually available on an unbundled basis. The FCC created new rules that permit competitive carriers to mix services that they lease from the incumbent carriers. We will now be able to mix incumbent carrier unbundled network elements with services purchased from the wholesale tariff (e.g., switched and special access services) instead of being required to artificially segregate unbundled network elements from such wholesale services. Because we currently lease both wholesale services and unbundled network elements from the incumbent carriers, we believe that these developments will result in cost savings for us.

- Calculation of Unbundled Element Rates: The TRO will allow incumbent carriers to utilize a higher cost of capital and shorter depreciation lives to establish rates for unbundled elements. We believe that these modifications could raise our costs for leasing unbundled network elements in the future.

Although the rules adopted by the FCC in the Triennial Review Order became effective on October 2, 2003, many of the requirements imposed by the FCC in the TRO were not self-executing. Accordingly, the FCC made clear that carriers must follow the change of law procedures in their applicable interconnection agreements to implement any TRO requirements that are not self-executing and that carriers must follow the procedures et forth in section 252(b) of the Telecom Act to modify interconnection agreements that are silent as to implementation of changes in law.

Several carriers and other entities appealed the FCC's TRO decision. On March 2, 2004, the U.S. Court of Appeals for the D.C. Circuit in Washington, D.C. issued its opinion in United States Telecom Associations v. FCC, No. 00-1012 ("USTA Decision"). In the USTA Decision, the court reversed and vacated many of the conclusions of the TRO. Specifically, the court found that the FCC improperly delegated to the states the overall responsibility for deciding whether certain unbundled elements should remain available to competitive carriers in each of the respective states. The FCC's determination in the TRO that competitive carriers should have access to switching platform services as a UNE ("UNE-P") was vacated by the court. The court also vacated the portions of the TRO which held that competitive carriers should have access to all forms of non-OC level unbundled dedicated transport.

XO does not rely on ILEC facilities to switch the majority of its customers' traffic and, therefore, will not be affected by the court's decision pertaining to UNE-P service, nor its likely impact on UNE-P providers if this decision is not reversed or stayed. Additionally, with the pending acquisition of Allegiance and its hundreds of collocation sites, we believe XO will lease less unbundled dedicated transport facilities from the ILECs. We expect these factors to mitigate the effects of any potential increases in the costs of leasing transport capacity.

The USTA Decision is stayed until May 1, 2004. Parties will seek review of the USTA Decision at the Supreme Court and will also seek a further stay of the decision. If the USTA Decision does go into effect and reverses and vacates large portions of the TRO, our ability to obtain access to certain unbundled network elements and incumbent network upgrades may be curtailed or more costly in the future. In addition, many incumbent carriers will continue to seek to institute follow-on administrative proceedings with the FCC and state regulatory agencies, and lobby the United States Congress, all in an effort to affect laws and regulations in a manner even more favorable to them and against the interests of competitive carriers. At the same time, we anticipate that competitive carriers will endeavor to improve their positions and access to the incumbents' networks through similar means. The final outcome of the appellate review and implementation process remains unknown at this time but it is possible that further changes to the rules could adversely affect our cost of doing business by increasing the cost of purchasing or leasing network facilities from the incumbent carriers.

Collocation in Incumbent Central Offices

Collocation regulations promulgated by the FCC specify in greater detail obligations that the Telecom Act imposes upon the incumbent carriers to open their local networks to competition by providing competitors space to locate their equipment in incumbent central offices and remote terminals for the purpose of interconnection. This allows the competitive carriers to provide local telephone services and to use portions of the incumbent carriers' existing networks to offer new and innovative services. Over the past four years, the FCC's collocation regulations have been the subject of very contentious proceedings at the FCC and litigation before several courts. On remand from a March 2000 decision by the U.S. Court of Appeals for the D.C. Circuit, the FCC issued a decision that revised its rules in a manner that permits incumbent companies to exercise more discretion in determining the placement of competitors' equipment in their central offices, and does not require the incumbents to allow competitors to install and maintain cross-connections between other collocated competitors, but requires the incumbent carriers to provide this as part of their collocation services. In June, 2002, the U.S. Court of Appeals for the D.C. Circuit affirmed the FCC's Remand Order, and the FCC has since clarified that incumbent carriers should make their cross-connection service available in the physical collocation tariffs they file with the FCC.

In October 2002, Verizon filed an application with the FCC requesting authority to discontinue providing new orders for federally-tariffed physical collocation services. Verizon asked the FCC to require its competitors instead to order collocation services going forward solely pursuant to terms and conditions approved by state public service commissions. Verizon's application was granted on October 22, 2003. This discontinuance will potentially make it more costly and difficult for competitors such as us to obtain new collocation services because the rates set by state public service commissions are typically significantly higher than those approved by the FCC, and may require competitors such as us to engage in costly and lengthy negotiations in different states.

Regulation of the RBOCs' Ability to Provide Long Distance Service

The FCC has primary jurisdiction over the implementation of Section 271 of the Telecom Act, which provides that the RBOCs cannot offer in-region long distance services until they have demonstrated that:

- they have entered into an approved interconnection agreement with a facilities-based competitive telephone company or that no such competitive telephone company has requested interconnection as of a statutorily determined deadline;
- they have satisfied a 14-element checklist designed to ensure that the RBOC is offering access and interconnection to all local exchange carriers on competitive terms; and
- the FCC has determined that allowing the RBOC to offer in-region, long distance services is consistent with the public interest, convenience and necessity.

As of December 15, 2003, the FCC has granted all of the RBOCs the authority to provide long distance service in every state in which they operate. All of the RBOCs now have the authority to bundle in-region long distance services with in-region local services. RBOC authorization to provide in-region long distance services could have an adverse effect on our ability to compete if effective post-approval safeguards are not enforced to ensure that the RBOCs continue to comply with the market-opening requirements.

Provision of Broadband Telecommunications Services and Information Services

Current federal and state regulation places certain restrictions and conditions on the provision of advanced telecommunications services, or broadband services, such as data and DSL services, by the RBOCs. Furthermore, the network elements that RBOCs must make available under the FCC's unbundling rules to competitors may be used for the provision of broadband services. However, at the urging of the RBOCs and other incumbent carriers, the FCC, in the TRO, appears to have greatly curtailed the extent to which the incumbents must unbundle the broadband portion of their networks for their competitors. The RBOCs continue to push for further deregulation through federal and state legislative efforts. In addition, it is anticipated that deregulatory legislation will be pursued by the RBOCs in Congress. In addition to possible legislation, the FCC has initiated another pending proceeding that could relax incumbent carriers' obligation to make unbundled network elements that are used for certain broadband or information services available to us. The FCC has issued a Notice of Proposed Rulemaking entitled "Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities" that requests comments on the proper classification of broadband access services as either regulated telecommunications services or unregulated information services. The TRO decision, in conjunction with a decision in this proceeding, a legislative change or a court ruling further broadening the definition of what constitutes unregulated information services could have the effect of allowing RBOCs to provide terms, conditions and pricing to their own affiliates that provide data or information services that are better than those made available to competitive carriers such as us. Such developments could also be expected to adversely affect our cost of doing business by increasing the cost of purchasing or leasing such facilities from the RBOCs.

Universal Service

In 1997, the FCC established a significantly expanded federal telecommunications subsidy regime known as "universal service". Specifically, the FCC established new subsidies for services provided to qualifying schools and libraries and rural health care providers, and expanded existing subsidies to low income consumers. Most telecommunications companies, including us, must pay for these programs based on their share of interstate and international telecommunications end user revenues. On December 4, 2003, the Wireline Competition Bureau released a public notice announcing that the proposed universal service contribution factor for the first quarter of 2004 is 8.7 percent compared to 9.5 percent for the third quarter of 2003 and 9.2 percent for the fourth quarter of 2003. The FCC has taken further steps to modify the system for assessment and recovery of universal service funds. In a December 2002 Notice of Proposed Rulemaking, the FCC asked many broad-ranging questions regarding universal service, including whether to change its method of assessing contributions due from carriers by basing it on the number and capacity of connections they provide, rather than on interstate and international end user revenues they earn. At this time, we are unable to predict whether the FCC's rulemaking or legislative initiatives will increase the size of our subsidy payments, the scope of the subsidy program, or our costs of calculating, collecting and remitting the universal service related payments.

Intercarrier Compensation Reform

Currently, telecommunications carriers are required to pay other carriers for interstate access charges and local reciprocal compensation charges. These two forms of Intercarrier compensation have been under review by the FCC since 2001. The FCC continues to consider a broad order reforming the Intercarrier compensation system and the following specific proceedings also impact Intercarrier compensation issues for us.

Access Charges. Long distance carriers pay local facilities-based carriers, including us, interstate access charges for both originating and terminating the interstate calls of long distance customers on the local carriers' networks. Historically, the incumbent carriers set access charges higher than cost and justified this pricing to regulators as a subsidy to the cost of providing local telephone service to higher cost customers. With the establishment of an explicit and competitively neutral universal service subsidy mechanism, however, the FCC is under increasing pressure to revise the current access charge regime to bring the charges closer to the actual cost of providing access. In response, the FCC issued a decision in 2001 setting interstate rates that competitive local carriers charge to long distance carriers at a level that will gradually decrease over three years from a maximum of $0.025 per minute to the rates charged by incumbent carriers. As long as we are in compliance with the FCC's rate schedule, the FCC's order forbids long distance carriers from challenging our interstate access rates. Although this FCC decision lowering access charges will reduce our access charge revenues over time, we do not expect that such a reduction will have a material impact on our total revenues or financial position. In 2001, the FCC also issued a declaratory ruling that commercial mobile radio service ("CMRS") providers are not permitted to collect switched access charges from long distance carriers absent a contract between the parties that imposes a payment obligation on the long distance carrier. In November 2003, the United States Court of Appeals for the District of Columbia denied petitions for review of the FCC's declaratory ruling on CMRS access charges. Sprint PCS and AT&T are currently litigating in federal district court in Missouri the issue of whether, in the absence of a written contract, Sprint PCS can charge AT&T for switched access services. We are unable to determine how the court will ultimately rule; however, if Sprint PCS prevails in this lawsuit against AT&T, it may encourage CMRS providers to attempt to collect switched access charges from us even in the absence of a written contract.

AT&T Declaratory Ruling Re: VoIP. AT&T has petitioned the FCC to find that voice over Internet protocol ("VoIP") services, including phone to phone services, are exempt from switched access charges. This proceeding has broad implications for the future of IP-based services because a ruling in favor of the AT&T petition will create incentives to deploy VoIP technology for the origination and termination of long distance and other calls. A ruling against the AT&T petition could place VoIP services in the same regulatory category as traditional telecommunications services and, therefore, subject VoIP services to access charges and other regulatory obligations including Universal Service fees. Like a growing number of carriers, we utilize Internet protocol technology for the transmission of a portion of our network traffic. The FCC has indicated on several occasions that such services are exempt from interstate access charges but, until the FCC issues its ruling in the current proceeding, it is unclear how such traffic will be treated for intercarrier compensation purposes. Additionally, several state commissions are in the process of addressing whether to regulate VoIP services, and this development could result in the emergence of inconsistent rules for intrastate VoIP services.

Vonage Petition. On September 22, 2003, Vonage Holdings, Inc. ("Vonage") filed a petition requesting that the FCC preempt an order of the Minnesota Public Utilities Commission ("PUC") requiring Vonage to comply with state laws governing providers of telephone service. The Minnesota PUC decision has been overturned by a Minnesota state court and now Vonage is seeking Federal preemption so that no future rulings of the Minnesota PUC can subject Vonage to state regulation. Vonage provides VoIP origination services to its customers and Vonage claims that it is therefore a provider of information services and not subject to traditional common carrier regulations. Specifically, Vonage asks that the FCC find that certain specific E911 requirements imposed by the Minnesota PUC are in conflict with federal policies. Further, Vonage states that preemption is necessary because of the impossibility of separating the Internet, or any service offered over it, into intrastate and interstate components. Until the FCC issues its ruling, it is unclear how VoIP offerings by XO and other companies will be regulated.

Level(3) Forbearance Petition. On December 23, 2003, Level(3) filed a petition for forbearance requesting the FCC to forbear from application of interstate or intrastate access charges on Internet protocol (IP) traffic that originates or terminates on the public switched telephone network (PSTN). IF the FCC were to rule in Level(3)'s favor, we would expect that there would be reductions in network and regulatory costs associated with the termination of certain IP-to-PSTN and PSTN-to-IP traffic.

Pulver.Com Ruling. On February 12, 2004, the FCC ruled that Pulver.Com's Free World Dialup (FWD) offering will remain a minimally regulated VoIP service. The Pulver.com Order made clear that IP-to-IP calls that do not transit over any portion of the PSTN will be largely free of regulation. Almost all of the calls carried by XO do transit some portion of the PSTN.

FCC VoIP NPRM. On February 12, 2004, the FCC initiated a major proceeding seeking public comment on a variety of issues based on the premise that Internet services and VoIP should remain largely free of regulatory burdens. In connection with this proceeding, the FCC will address VoIP-related Communications Assistance for Law Enforcement (CALEA) issues to address the technical aspects of enabling law-enforcement access to IP-enabled services. At this time it is unclear how, if at all, the FCC will regulate IP-enabled service including VoIP.

Local Reciprocal Compensation Charges. Local telephone companies such as us that originate traffic that is terminated on the network of other carriers typically compensate the other local carriers for terminating that traffic. These payments flow in both directions between any two carriers. First, when we terminate traffic for another local carrier to a customer on our network, we collect compensation. Second, when we send our customers' traffic to another carrier for termination, we pay compensation. Some competitors, however, have a customer base that generates many more minutes of terminating traffic from other carriers than originating traffic destined for other carriers. For example, a competitor that has a customer base that has many information service providers typically will have a large amount of compensation being paid to it by other carriers, while it will owe very little reciprocal compensation to other carriers. The FCC revamped the local reciprocal compensation structure in 2001 on an interim basis for three years to eliminate or reduce the opportunity for carriers to take advantage of an imbalance of originating and terminating traffic flows due to traffic terminated to information service providers. The FCC also initiated a rulemaking to examine inter-carrier compensation more comprehensively. Under the decision, at the election of the incumbent carrier, terminating traffic that is out-of-balance by a ratio of more than 3 to 1 can be compensated at a lower rate, or in some cases, at no charge. This ruling allows us to continue to collect reciprocal compensation payments from other carriers since we have an imbalance in the amount of traffic we terminate versus the amount we originate. Going forward, an adverse ruling in the general intercarrier compensation reform proceeding could end reciprocal compensation payments and eliminate this line of revenue for us.

TELRIC Proceeding. On September 10, 2003, the FCC initiated a new proceeding to consider significantly revamping the current Total Element Long Run Incremental Cost ("TELRIC") methodology used for the pricing of unbundled network elements. An adverse ruling in the new proceeding will allow the incumbent carriers to increase unbundled network element rates and this would raise our costs for leasing unbundled network elements in the future. A decision is expected sometime in 2004. Several State Commissions have also initiated proceedings to review the rate levels that the incumbent carriers charge for unbundled network elements. An adverse ruling in these proceedings would allow the incumbent carriers to increase unbundled network element rates in the applicable state and this would raise our costs for leasing unbundled network elements in the future.

LMDS Auction. On July 28, 2004, the FCC plans to initiate an auction of spectrum in the 24 GHz band. The 24 GHz band consists of the bands 24.25-24.45 GHz and 25.05-25.25 GHz. Five licenses, each with two paired 40 MHz blocks, will be offered in each of 176 geographic areas. Stations in the 24 GHz Service may render any kind of digital fixed communications service. Auction winners will be required to protect incumbent licensees. Virtually all of the incumbent licenses are held by Teligent, Inc. in a variety of areas throughout the country. The winning bidder for the 24 GHz service may use these stations to provide services in competition with those offered by XO, although the 24 GHz bands consist of less spectrum than that for which XO is licensed to provide LMDS service.

Nasdaq Listing

On February 4, 2004, we announced our intention to begin the process of applying for the listing of shares of our New Common Stock on The Nasdaq National Market. Shares of our New Common Stock will continue to be quoted on the OTCBB until the Nasdaq application is approved. See Item 5 "Market for Registrant's Common Equity and Related Stockholder Matters."

If our shares become listed on the Nasdaq National Market, we will be required to comply with the Nasdaq Marketplace Rules, which, as required by the Sarbanes-Oxley Act of 2002, contain corporate governance requirements in addition to those contemplated by the Delaware General Corporation Law and the Federal Securities Laws, including requirements related to:

- Distribution of interim reports
- Solicitation of proxies
- Independent directors
- Audit committees
- Shareholder approval
- Stockholder voting rights
- Auditor peer review

Employees

As of December 31, 2003 we employed approximately 5,100 people, including full-time and part-time employees. In March 2004, our headcount was approximately 4,500 as we managed costs out of the business. Overall, we consider our employee relations to be good. None of our employees are covered by a collective bargaining agreement.

Risk Factors

Risks Related to Our Operations

The failure of our operations support systems, including the systems for sales tracking, order entry and provisioning, and billing that we are currently in the process of updating and replacing, to perform as we expect could impair our ability to retain customers and obtain new customers, or provision their services, or result in increased capital expenditures, which would adversely affect our revenues or capital resources.

Our operations support systems are an important factor in our operations. Critical information systems used in daily operations perform sales and order entry, provisioning, billing and accounts receivable functions, and cost of service verification and payment functions, particularly with respect to facilities leased from ILECs. If any of these systems fail or do not perform as expected, such failures would impact our ability to process orders and provision sales, and to bill for services efficiently and accurately, which could, in turn, cause us to suffer customer dissatisfaction, loss of business or the inability to add new customers or additional services to existing customers in a timely basis, any of which would adversely affect our revenues. In additional, system failure or performance issues could impact our ability to effectively audit and dispute invoicing and provisioning data provided by service providers from whom we lease facilities.

We believe that our Disaster Recovery framework to control and address systems risks is not fully redundant, and we may incur the costs, delays and customer complaints associated with system failures. In addition, our ability to efficiently and accurately provision new orders for services on a timely basis is necessary for us to begin to generate revenue related to those services. We have experienced, and may continue to experience, delays and related problems in processing service orders, provisioning sales and billing in connection with the transition to these new systems. If the delays or related problems continue, or if any unforeseen problems emerge in connection with our migration to the new provisioning software and systems, delays and errors may occur in the provisioning process, which could significantly increase the time until an order for new service can begin to generate revenue, which could have a material adverse effect on our operations.

Our rights to the use of the unlit capacity that make up our network may be affected by the financial health of our fiber providers.

We possess the right to use the unlit capacity that is included in our network, particularly in our intercity network, through long-term leases or indefeasible right of use agreements. A bankruptcy or financial collapse of one of these fiber providers could result in a loss of our rights under such leases and agreements with the provider, which in turn could have a negative impact on the integrity of our network, our ability to expand the capacity of our network as our business grows, and ultimately on our results of operations. For example, we lease or have indefeasible rights of use on networks owned and maintained by Level 3 Communications. If Level 3 were to encounter financial difficulties, we may not be able to maintain, or protect our rights in important components of our intercity network. In such an event, there can be no assurance that we will be able to lease comparable strands of unlit capacity if we are not able to retain our rights to use the existing unlit capacity we have obtained from Level 3, nor that we will be able to lease such strands from another provider at competitive or economical rates.

We may not be able to continue to connect our network to the incumbent carrier's network or maintain Internet peering arrangements on favorable terms, which would impair our growth and performance.

We are required to be a party to interconnection agreements with the incumbent carrier and certain independent carriers or ILECs in order to connect our customers to the public telephone network. If we are unable to renegotiate or maintain interconnection agreements in all of our markets on favorable terms, it could adversely affect our ability to provide services in the affected markets.

Peering agreements with Internet service providers allow us to access the Internet and exchange transit with these providers. Depending on the relative size of the carriers involved, these exchanges may be made without settlement charge. Recently, many Internet service providers that previously offered peering have reduced or eliminated peering relationships or are establishing new, more restrictive criteria for peering and an increasing number of these service providers are seeking to impose charges for transit. Increases in costs associated with Internet and exchange transit could have a material adverse effect on our margins for our products that require Internet access. We may not be able to renegotiate or maintain peering arrangements on favorable terms, which would impair our growth and performance.

If our selection of IP technology is incorrect, ineffective or unacceptably costly, implementation of our business strategy could be delayed, which would adversely affect our growth and operating results.

We rely on IP technology as the basis for our metro and intercity networks. Integrating this technology into our network may prove difficult and may be subject to delays. In addition, affordable IP customer premise equipment may not become available in a timely fashion, if at all. If the technology choices we make prove to be incorrect, ineffective or unacceptably costly, our strategy of meeting our customer's demand for existing and future telecommunications services using IP technology could fail, which would adversely affect our growth and operating results.

We may be unable to adequately protect our intellectual property or rights to licenses for use of third-party intellectual property, and may be subject to claims that we infringe the intellectual property of others, which could substantially harm our business.

We rely on a combination of patents, copyrights, and other proprietary technology that we license from third parties. We have been issued several United States and foreign trademarks and may consider abandoning some trademarks and/or filing for additional trademarks in the future. We have also been issued one United States patent and may consider filing for additional patents in the future, however, we cannot assure you that any additional patents or trademarks will issue or that our issued patent or trademarks will be upheld in all cases. We cannot guarantee that these and other intellectual property protection measures will be sufficient to prevent misappropriate of our trademark or technology or that our competitors or licensors will not independently develop technologies that are substantially equivalent to or superior to ours. In addition, the legal systems in many other countries do not protect intellectual property rights to the same extent as the legal system of the United States. If we are unable to adequately protect our proprietary interests and business information or our present license arrangements, our business, financial condition and results of operations could be materially adversely affected. Further, the dependence of the communications industry on proprietary technology has resulted in frequent litigation based on allegations of the infringement of patents and other intellectual property. In the future, we may be subject to litigation to defend against claimed infringement of the rights of others or to determine the scope and validity of the proprietary rights of others. Future litigation also may be necessary to enforce and protect our trade secrets and other intellectual property rights. Any intellectual property litigation could be costly and cause diversion of our management's attention from the operation of our business. Adverse determinations in any litigation could result in the loss of proprietary rights, subject us to significant liabilities or require us to seek licenses from third parties that may be available on commercially reasonable terms, if at all. We could also be subject to court orders preventing us from providing certain services in connection with the delivery of our services to our customers.

Risks Related to Liquidity, Financial Resources, and Capitalization

We incurred a substantial net loss in 2003 and, in the near term, will not generate funds from operations sufficient to meet all of our cash requirements.

For each period since inception, we have incurred substantial net losses. For 2003, we posted a net loss attributable to common stockholders of approximately $102.6 million. In the near term, we expect to use cash to fund our expected operating losses, and our ongoing capital expenditure requirements.

As a result of our commitment to purchase substantially all of the assets of Allegiance, we have committed to expend a majority of the cash reflected on our balance sheet as of December 31, 2003, and, as a result, we may be required to seek additional capital to fund our operations.

As discussed above, we have committed to purchase substantially all of the assets of Allegiance for an aggregate purchase price that includes approximately $311.0 million in cash. If the Allegiance asset acquisition had been consummated immediately prior to the end of our most recently ended fiscal year, we would have had approximately $209.6 million in cash, cash equivalents and marketable securities on our balance sheet as of December 31, 2003. We believe that, upon the consummation of the Allegiance asset acquisition, our remaining cash and cash equivalents as of that date will be significantly less than that figure based upon our need to fund our ongoing losses from operations. If we are required to use a significant amount of our remaining cash to repay some or all of our outstanding debt or to fund any unforeseen, necessary capital expenditures, we may lack sufficient cash to continue to fund our losses from operations. We cannot assure you that we will be able to obtain additional financing. Even if we could obtain additional financing, we cannot assure you that it would be on terms that are favorable to us. If we cannot obtain additional financing when needed, this would have a material adverse effect on us.

The covenants in our Credit Agreement restrict our financial and operational flexibility, which could have an adverse affect on our results of operations.

Our Credit Agreement contains covenants that restrict, among other things, the amount of our capital expenditures, our ability to borrow money, grant additional liens on our assets, make particular types of investments or other restricted payments, sell assets or merge or consolidate. A company controlled by Mr. Carl Icahn holds more than 90% of the principal amount of the loans outstanding under the Credit Agreement. Because amendments to or waivers of covenants under the Credit Agreement generally require the approval or consent of holders of only a majority of the outstanding principal amount under the Credit Agreement, decisions whether to amend or waive compliance with such covenants by the holders of loans under the Credit Agreement can be made by Mr. Icahn, whether or not the other holders agree.

The security for the Credit Agreement consists of substantially all of the assets of XO Parent and our subsidiaries. A default under the Credit Agreement could adversely affect our rights under other commercial agreements.

The Credit Agreement and the existence of the loans under the Credit Agreement also could affect our financial and operational flexibility, as follows:

- they may impair our ability to obtain additional financing in the future;
- they may limit our flexibility in planning for or reacting to changes in market conditions; and
- they may cause us to be more vulnerable in the event of a downturn in our business.

Risks Related to the Acquisition of the Allegiance Assets

We may not successfully consummate the acquisition of the Allegiance assets.

Our acquisition of substantially all of the assets of Allegiance, although approved by the U.S. Bankruptcy Court, remains contingent upon fulfillment of a variety of covenants contained in the definitive documentation pursuant to which we anticipate acquiring the Allegiance assets. Such contingencies include, without limitation, our obtaining regulatory clearances, such as Hart-Scott-Rodino clearance and approval of the FCC and state public utility commissions. There can be no assurance that we will obtain the governmental approvals and clearances required to consummate our acquisition of the Allegiance assets. If we are not able to consummate the acquisition of the Allegiance assets, then we will not be able to realize the improvements in our network infrastructure and resulting competitive advantages associated with our ownership of the Allegiance assets.

We may not realize the network and selling, operating, and administrative synergies that we estimate in connection with the acquisition of the Allegiance assets.

While we are confident that we have correctly estimated the potential network and selling, operating, and administrative synergies that we can realize in connection with the acquisition of the Allegiance assets, it is possible that our estimates could prove to be incorrect. For example, we may discover during the process of integrating the Allegiance assets into our network and business infrastructures that some of the acquired assets require greater maintenance or earlier replacement than originally anticipated. In addition, unanticipated growth in our business as a result of the acquisition of the Allegiance assets may require that some facilities or support functions that we currently anticipate will be combined or reduced may be necessary to retain for us to maintain our operations. The synergies that we anticipate to realize are also dependent on our ability to combine the Allegiance assets with our own network infrastructure in a manner that permits us to realize those synergies. If we have not estimated the potential synergies correctly, or if we are not able to integrate the Allegiance assets into our network infrastructure effectively, we may not realize any synergies in connection with the acquisition of the Allegiance assets, or such synergies may take longer to realize.

Risks Related to Competition and Our Industry

Technological advances and regulatory changes are eroding traditional barriers between formerly distinct telecommunications markets, which could increase the competition we face and put downward pressure on prices, which could impair our results.

New technologies, such as voice-over-IP, and regulatory changes — particularly those permitting incumbent local telephone companies to provide long distance services — are blurring the distinctions between traditional and emerging telecommunications markets. In addition, the increasing importance of data services has focused the attention of most telecommunications companies on this growing sector. As a result, a competitor in any of our business areas is potentially a competitor in our other business areas, which could impair our prospects, put downward pressure on prices and adversely affect our operating results.

We face competition in each of our markets principally from the incumbent carrier in that market, but also from recent and potential market entrants, including long distance carriers seeking to enter, reenter or expand entry into the local exchange marketplace and incumbent carriers seeking to enter into the long distance market as they are granted the regulatory authority to do so. This competition places downward pressure on prices for local and long distance telephone service and data services, which can adversely affect our operating results. In addition, we could face competition from other companies, such as other competitive carriers, cable television companies, microwave carriers, wireless telephone system operators and private networks built by large end-users. We are much smaller in size and resources than many of our competitors. If we are not able to compete effectively with these industry participants, our operating results could be adversely affected.

Our company and industry are highly regulated, which restricts our ability to compete in our target markets and imposes substantial compliance costs on us that adversely impact our results.

We are subject to varying degrees of regulation from federal, state and local authorities. This regulation imposes substantial compliance costs on us. It also restricts our ability to compete. For example, in each state in which we desire to offer our services, we are required to obtain authorization from the appropriate state commission. If any required authorization for any of our markets or services is revoked or otherwise terminated, our ability to operate in the affected markets would be adversely affected.

Attempts to limit the basic competitive framework of the Telecom Act could interfere with the successful implementation of our business plan.

Successful implementation of our business plan is predicated on the assumption that the basic framework for competition in the local exchange services market established by the Telecom Act will remain in place. We expect that there will be attempts to limit or eliminate this basic framework through a combination of federal legislation, new rulemaking by the FCC and challenges to existing and proposed regulations by the RBOCs. It is not possible to predict the nature of any such action or its impact on our business and operations.

Risks Related to Our New Common Stock

An entity owned and controlled by Mr. Carl C. Icahn is our majority stockholder.

An entity owned and controlled by Mr. Carl C. Icahn, Chairman of our board of directors, has filed a Form 13D with the Securities and Exchange Commission indicating that it owns over 60% of our outstanding New Common Stock as of January 31, 2004. As a result, Mr. Icahn has the power to elect all of our directors. Under applicable law and our certificate of incorporation and by-laws, certain actions cannot be taken without the approval of holders of a majority of our voting stock including, without limitation, mergers and the sale of substantially all of our assets and amendments to our certificate of incorporation and by-laws. We anticipate that Mr. Icahn will continue to control a majority of our outstanding capital stock following the issuance of XO Parent shares in connection with our acquisition of Allegiance assets and consequently will continue to have these governance rights.

Future sales of our New Common Stock could adversely affect its price and/or our ability to raise capital.

Future sales of substantial amounts of New Common Stock, or the perception that such sales could occur, could adversely affect the prevailing market price of the New Common Stock and our ability to raise capital.

As of February 20, 2004, there were 136,510,535 shares of New Common Stock outstanding. The shares of New Common Stock owned by an entity owned and controlled by Mr. Icahn, are restricted shares that may be sold only under a registration statement or an exemption from federal securities registration requirements. Mr. Icahn, through various entities that he owns or controls, has the right to require XO to register, under the Securities Act of 1933, shares of New Common Stock held by such entities and to include shares of New Common Stock held by them in certain registration statements filed by XO, pursuant to a Registration Rights Agreement approved by the Bankruptcy Court in connection with the Company's Chapter 11 proceedings.

Pursuant to our Plan of Reorganization, we have issued three series of warrants to purchase up to an aggregate of approximately 9.5 million, 7.1 million and 7.1 million additional shares of New Common Stock, at exercise prices of $6.25, $7.50 and $10.00 per share, respectively. The warrants will expire on January 16, 2010.

We have options outstanding to purchase approximately 9.5 million shares of New Common Stock outstanding under our 2002 Stock Incentive Plan as of February 20, 2004. Unless surrendered or cancelled earlier under the terms of the stock incentive plan, those options will expire beginning in 2013. In addition, our stock incentive plan authorizes future grants of options to purchase New Common Stock, or awards of restricted New Common Stock, with respect to an additional 6.3 million shares of New Common Stock in the aggregate.

Other Risks

There may be risks related to our use of Arthur Andersen as our independent auditors for the year ended December 31, 2001 and prior periods.

Arthur Andersen, LLP, our former independent public accountants, which audited our financial statements for the year ended December 31, 2001, was found guilty on June 15, 2002 of federal obstruction of justice charges in connection with the federal government's investigation of Enron Corp. Arthur Andersen ceased practicing before the SEC effective August 31, 2002. Based on our understanding of Arthur Andersen's financial condition, it may be unable to satisfy any claims that arise out of its provision of auditing and other services to us, including claims that may arise out of Arthur Andersen's audits of our consolidated financial statements in years prior to 2002. The SEC has said that it will continue to accept financial statements audited or reviewed by Arthur Andersen in compliance with applicable rules and orders issued by the SEC in March 2002 in connection therewith.

Forward-Looking Statements

Our forward-looking statements are subject to a variety of factors that could cause actual results to differ significantly from current beliefs.

Some statements and information contained in this Annual Report on Form 10-K are not historical facts, but are "forward-looking statements," as such term is defined in the Private Securities Litigation Reform Act of 1995. These forward-looking statements can be identified by the use of forward-looking terminology such as "believes," "expects," "plans," "may," "will," "would," "could," "should," or "anticipates" or the negative of these words or other variations of these words or other comparable words, or by discussions of strategy that involve risks and uncertainties. Such forward-looking statements include, but are not limited to, statements regarding:

- our services, including the development and deployment of data products and services based on IP, Ethernet and other technologies and strategies to expand our targeted customer base and broaden our sales channels;
- the operation of our network, including with respect to the development of IP protocols;
- liquidity and financial resources, including anticipated capital expenditures, funding of capital expenditures and anticipated levels of indebtedness; and
- trends related to and expectations regarding the results of operations in future periods, including but not limited to those statements set forth in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations below.

All such forward-looking statements are qualified by the inherent risks and uncertainties surrounding expectations generally, and also may materially differ from our actual experience involving any one or more of these matters and subject areas. The operation and results of our business also may be subject to the effect of other risks and uncertainties, in addition to the relevant qualifying factors identified in the above "Risk Factors" section and elsewhere in this annual report and in the documents incorporated by reference in this annual report, including, but not limited to:

- general economic conditions in the geographic areas that we are targeting for communications services;
- the ability to achieve and maintain market penetration and average per customer revenue levels sufficient to provide financial viability to our business;
- the quality and price of similar or comparable communications services offered or to be offered by our current or future competitors; and
- future telecommunications-related legislation or regulatory actions.

Item 2. Properties

We own or lease, in our 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. Our central office switching equipment includes electronic switches and peripheral equipment.

The fiber optic backbone and distribution network and connecting lines include aerial and underground cable, conduit, poles and wires. These facilities are located on public streets and highways or on privately-owned land. We have permission to use these lands pursuant to consent or lease, permit, easement, or other agreements.

We, and our subsidiaries, lease facilities for our and their administrative and sales offices, central switching offices, network nodes and warehouse space. The various leases expire in years ranging from 2004 to 2029. Most have renewal options.

Our headquarters are located in Reston, Virginia, where we are currently leasing approximately 170,000 square feet of space. In February 2003, Dixon Properties, LLC, which is owned by Mr. Carl Icahn, acquired ownership of the building in which our headquarters is located in a transaction that was approved by the Bankruptcy Court in our Chapter 11 proceedings.

Item 3. Legal Proceedings

XO is involved in lawsuits, claims, investigations and proceedings consisting of commercial, securities, tort, and employment matters, which arise in the ordinary course of business. In addition, disputes with respect to general unsecured claims and two administrative claims against XO Parent in the aggregate amount of approximately $23.0 million remain pending from the XO Parent Chapter 11 proceedings. In accordance with SFAS No. 5, "Accounting for Contingencies," XO makes a provision for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. XO believes it has adequate provisions for any such matters. XO reviews these provisions at least quarterly and adjusts these provisions to reflect the impacts of negotiations, settlements, rulings, advice of legal counsel, and other information and events pertaining to a particular case. Litigation is inherently unpredictable. However, XO believes that it has valid defenses with respect to legal matters pending against it. Nevertheless, it is possible that cash flows or results of operations could be materially affected in any particular period by the unfavorable resolution of one or more of these contingencies.

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

No matter was submitted to a vote of security holders during the fourth quarter.

PART II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters

Our New Common Stock began trading shortly after our Effective Date and is quoted on the OTCBB under the symbol "XOCM.OB." According to the records of our transfer agent, we had 68 stockholders of record as of February 20, 2004. The majority of our shares that are held by non-affiliates are held in approximately 9,000 customer accounts held by brokers and other institutions on behalf of stockholders. However, we believe that the total number of non-affiliated stockholders is less than 9,000 due to stockholders with accounts at more than one brokerage. During 2002, our pre-petition stock traded on Nasdaq under the symbol "XOXO." The following table sets forth the low and high sale price of our common stock, based on the last daily sale, in each of our last eight fiscal quarters.

	2003		2002	
	High	Low	High	Low
First Quarter	$4.00	$0.35	$0.19	$0.04
Second Quarter	$7.80	$3.90	$0.07	$0.02
Third Quarter	$8.33	$5.60	$0.08	$0.02
Fourth Quarter	$5.80	$4.97	$0.15	$0.02

All of the 2003 over-the-counter market quotations set forth in this table reflect inter-dealer quotations, without retail mark-up, mark-down, or commission and may not necessarily reflect actual transactions. Our secured Credit Facility prohibits the payment of cash dividends.

Information pertaining to XO's equity compensation plans is set forth in XO's Proxy Statement, to be filed within 120 days after XO's year end of December 31, 2003, which information is incorporated herein by reference.

Item 6. Selected Financial Data

Because the Plan of Reorganization was not consummated and effective until January 16, 2003, the predecessor selected consolidated financial data below as of and for the years ended December 31, 2002, 2001, 2000, and 1999 does not include the effects of the fresh start accounting provisions of SOP 90-7. The reorganized selected consolidated financial data as of and for the year ended December 31, 2003 reflects the impact of adopting fresh start and is not comparable to that of predecessor XO. Fresh start required that XO adjust the historical cost of its assets and liabilities to their fair values as determined by the reorganization value of the Company. We engaged an independent appraiser to assist in the allocation of the reorganization value to the reorganized Company's assets and liabilities by determining the fair market value of its property and equipment, intangible assets and certain obligations related to its facility leases. Although the effective date of the Plan of Reorganization was January 16, 2003, due to the immateriality of the results of operations for the period between January 1, 2003 and the effective date, XO has accounted for the consummation of the Plan of Reorganization as if it had occurred on January 1, 2003 and implemented fresh start as of that date. The accounting impact from adopting fresh start follows immediately after the selected financial data table (dollars in thousands, except share data).

	Reorganized XO	Predecessor XO			
	Year Ended December 31,	Year Ended December 31,			
	2003	2002	2001	2000(a)	1999
Statement of Operations Data:					
Revenue	$1,110,483	$ 1,259,853	$ 1,258,567	$ 723,826	$ 274,324
Loss from operations (b)	(111,858)	(1,208,898)	(1,949,891)	(1,011,652)	(366,530)
Net loss (c)	(102,554)	(3,386,818)	(2,086,125)	(1,101,299)	(558,692)
Net loss applicable to common shares (c) (d)	(102,554)	(3,350,362)	(1,838,917)	(1,247,655)	(627,881)
Net loss per common share, basic and diluted (e)	(1.07)	(7.58)	(4.55)	(3.87)	(2.51)
Statement of Cash Flow Data:					
Net cash provided by (used in) operating activities	$ 6,301	$ 17,602	$ (560,877)	$ (559,414)	$ (349,192)
Net cash provided by (used in) investing activities	153,036	57,582	(708,598)	(1,464,495)	(1,050,344)
Net cash (used in) provided by financing activities	5,185	(6,079)	1,019,647	1,648,663	1,948,503
Balance Sheet Data:					
Cash, cash equivalents and marketable securities	$ 520,612	$ 560,983	$ 755,167	$ 1,860,963	$ 1,881,764
Property and equipment, net	485,984	2,780,589	3,742,577	2,794,105	1,180,021
Broadband wireless licenses and other intangibles, net (c)	109,515	984,614	2,977,575	3,912,209	1,017,817
Total assets (c)	1,265,165	4,585,496	7,930,465	9,085,375	4,597,108
Total long-term debt and accrued interest payable (f)	536,791	5,165,718	5,109,503	4,396,596	3,733,342
Redeemable preferred stock, net of issuance costs (d)	—	1,708,316	1,781,990	2,097,016	612,352
Total stockholders' equity (deficit) (f)	380,425	(3,032,282)	297,416	1,838,401	(13,122)

(a) The selected consolidated financial data includes the accounts and activities of Concentric Network Corporation since June 16, 2000, the date that we merged with Concentric.

(b) In 2002, loss from operations included non-cash charges totaling $477.3 million in connection with the amendment to the terms of fiber acquisition and maintenance arrangements with Level 3 Communications, and the return of previously acquired intercity fiber in connection therewith. In 2001, loss from operations included restructuring charges totaling $509.2 million associated with the restructuring of certain aspects of our business operations. Loss from operations in 1999 included restructuring charges totaling $30.9 million associated with relocating our Bellevue, Washington headquarters to Reston, Virginia.

(c) In 2003, net loss included a $33.5 million gain on investment sales. In 2002, net loss and total assets reflects a $1,876.6 million impairment charge to write-off all of our goodwill as a cumulative effect of accounting change, pursuant to SFAS No. 142. In 2001, net loss included a gain of $345.0 million resulting from the repurchase of certain of our senior notes. In 2000, net loss included a $225.1 million net gain from the sale of an equity investment.

(d) The comparability of net loss applicable to common shares is impacted by the transactions discussed in c. above. In 2001, net loss applicable to common shares includes a gain of $376.9 million resulting from the repurchase of certain of our preferred stock.

(e) The net loss per share data for the years ended December 31, 2002, 2001, 2000, and 1999 has been calculated based on the shares outstanding of our class A and class B common stock prior to the consummation of our Plan of Reorganization. Effective January 16, 2003, the effective date of the Plan of Reorganization, all interests in our class A and class B common stock were terminated and all outstanding shares were cancelled. For further discussion of our Plan of Reorganization, see "Business — Our Reorganization". The net loss per share data for the years ended December 31, 2000 and 1999 has been adjusted for the splits of our class A and class B common stock effected in 2000.

(f) In January 2004, we completed a rights offering as part of our Plan of Reorganization. An aggregate of 39.7 million shares were issued in the offering, yielding net proceeds of $197.6 million. These proceeds were used to pay down our long-term debt and accrued interest payable.

Fresh start accounting adjustments

A reconciliation of the adjustments recorded in connection with our reorganization and the adoption of fresh start is presented below (dollars in thousands):

	Predecessor XO December 31, 2002	Reorganization	Fresh Start Adjustments (d)	Reorganized XO January 1, 2003
ASSETS				
Current assets:				
Cash and cash equivalents	$ 314,038	$ —	$ —	$ 314,038
Marketable securities	246,945	—	—	246,945
Accounts receivable, net	116,541	—	—	116,541
Other current assets	83,480	—	(48,288)	35,192
Total current assets	761,004	—	(48,288)	712,716
Property and equipment, net	2,780,589	—	(2,304,001)	476,588
Broadband wireless licenses and other intangibles, net	984,614	—	(848,936)	135,678
Other assets, net	59,289	—	(36,181)	23,108
Total assets	$ 4,585,496	$ —	$(3,237,406)	$1,348,090
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY				
Current liabilities:				
Accounts payable	$ 63,729	$ —	$ 3,539	$ 67,268
Accrued liabilities	266,102	—	(30,910)	235,192
Current liabilities subject to compromise	5,497,207	(5,466,667) (a)	(30,540)	—
Total current liabilities	5,827,038	(5,466,667)	(57,911)	302,460
Long-term debt	—	500,000 (b)	—	500,000
Other long-term liabilities	75,242	—	(4,612)	70,630
Long-term liabilities subject to compromise	7,182	—	(7,182)	—
Total liabilities	5,909,462	(4,966,667)	(69,705)	873,090
Predecessor XO redeemable preferred stock — subject to compromise	1,708,316	(1,708,316) (a)	—	—
Stockholders' (deficit) equity:				
Predecessor XO common stock	4,628,139	—	(4,628,139)	—
Reorganized XO common stock and warrants	—	475,000 (c)	—	475,000
Deferred compensation	(8,500)	—	8,500	—
Accumulated other comprehensive income	2,512	—	(2,512)	—
Accumulated deficit	(7,654,433)	6,199,983 (e)	1,454,450	—
Total stockholders' (deficit) equity	(3,032,282)	6,674,983	(3,167,701) (e)	475,000
Total liabilities and stockholders' (deficit) equity	$ 4,585,496	$ —	$(3,237,406)	$1,348,090

(a) To record the discharge of pre-petition indebtedness, including a $1.0 billion credit facility, $4.2 billion of senior and convertible subordinated notes, $245.2 million of accrued interest, and the elimination of $1.7 billion of pre-petition redeemable preferred stock and accrued dividends, all in accordance with the Plan of Reorganization.

(b) To record the outstanding principal under the Credit Agreement, in accordance with the Plan of Reorganization.

(c) To record the issuance of 95.0 million shares of New Common Stock and warrants in accordance with the Plan of Reorganization. Participation in the Rights Offering was recorded in the first quarter of 2004.

(d) To adjust the carrying value of assets, liabilities and stockholders' equity to fair value.

(e) Net reorganization gain on January 1, 2003 consisted of the following (dollars in thousands):

Net gain resulting from reorganization of debt, preferred stock and equity	$ 6,199,983
Net loss resulting from fresh start fair value adjustments to assets and liabilities	(3,167,701)
Total reorganization gain, net	$ 3,032,282

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

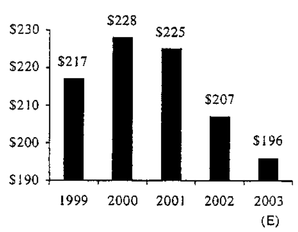
Executive Overview of Our Business

State of the Telecommunications Industry

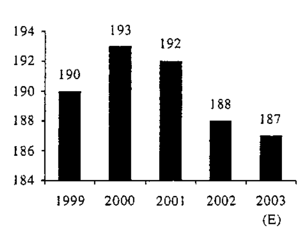
In general, growth in the telecommunications industry has been sluggish for the past three years. Demand for some services, such as wireless and integrated product offerings have increased, but for many other products and services price compression and lower demand have resulted in year over year revenue declines for many telecommunication companies. The weakened US economy caused our industry to experience:

- Reduced new customer demand and/or reductions in existing customer services,
- High number of bankruptcies in the telecommunications industry and the economy in general,
- Continued competitive pressures, including price cutting in some product lines,
- Reduced FCC mandated rates.

The telecommunications industry annual revenues peaked for wireline services in 2000 at $228 billion, and are estimated to be approximately $196 billion in 2003. Associated lines have declined from 193 million in 2000 to an estimated 187 million in 2003.



Source: *Local Competition Report* (FCC, 2004)



Source: *Trends in Telephone Service* (FCC, 8/03)

As a result of over-investment, increased debt-loads, and financial downturn, the telecommunications industry saw record numbers of bankruptcies in 2001 and 2002. Some companies survived and emerged with much smaller debt loads, while others were liquidated.

We were one of the companies that successfully emerged from bankruptcy at the beginning of 2003 with a much smaller debt load. We believe that our revenue decline from 2002 to 2003 is consistent with that of other competitive local exchange carriers. In addition to the loss of customers and related revenues, excess capacity and competitive pricing pressures caused us to reduce prices when selling certain long distance voice services. Excess long haul capacity has not, however, caused similar pricing pressures when selling other services. There has also been an increasing displacement of basic wireline services due to growth in wireless phone usage. This trend is expected to increase in 2004.

Business Overview

We provide a comprehensive array of voice and data communications services to business customers. These services are offered to a variety of customers, including small, middle-market and large commercial businesses, and carrier or wholesale customers in over 70 U.S. markets. Our voice services include local and long distance services, both bundled and standalone, other voice-related services such as conferencing, calling card, domestic and international toll free services, advanced directory services, Hosted IVR and transactions processing services for prepaid calling cards. Our data services include Internet access, including Dedicated Internet Access, DSL and dial access, private data networking, including Ethernet service, Wavelength service, MultiTransport Networking Service and managed security solutions including Virtual Private Network and firewall services, and web hosting services. We also combine many of these services in flat rate service packages.

Key Performance Indicators

Management uses various key performance indicators or KPIs to assess operational effectiveness in certain areas. These include:

- Sales activity — This KPI tracks the dollar value of sales bookings and quota attainment per sales representative. Management reviews this metric to assess the effectiveness of our sales force, and to track the sales backlog to be installed.
- Customer attrition or churn — This KPI tracks the financial impact of customer attrition, or churn, in comparison to new sales. Management reviews this KPI to judge the effectiveness of operational measures intended to promote customer satisfaction with our services, and the net impact on revenue.
- Number and average dollar of customer orders processed — This KPI tracks the quantity and size of customer installations, changes or disconnects that we have processed in a particular period.

System Conversions

As noted in the liquidity section below, we are investing significant capital into the continued development and implementation of our information systems to support and enhance the provisioning and billing of new and existing customers. There are four major components to our customer management and billing systems: (i) sales ordering and customer management (sometimes referred to as CRM); (ii) provisioning support system; (iii) billing systems; and (iv) integration of the above systems. Integration is the ability to automate the flow of information between systems, resulting in fewer errors, reduced intervals and lower headcount costs to order, install and manage the customer base. We installed the provisioning system in 2003. In early 2004, we installed a new CRM system. We expect to install a new billing system in 2004 and complete an integration release to provisioning in the second quarter of 2004, and an integration release to billing in the third quarter of 2004. If we are successful at implementing these systems we will experience operating efficiencies starting in the second half of 2004 and into 2005.

Our Chapter 11 Reorganization

The Reorganization Proceedings

On January 16, 2003, XO Parent consummated its Plan of Reorganization and emerged from its Chapter 11 reorganization proceedings with a significantly restructured balance sheet. The consummation of the Plan of Reorganization resulted in the following changes in XO Parent's capital structure:

- The conversion of $1.0 billion of loans under our pre-petition secured credit facility into $500.0 million of outstanding principal amount under an amended and restated credit agreement;
- The extinguishment of all amounts due under our pre-petition unsecured senior and subordinated notes and certain general unsecured obligations;
- The cancellation of all outstanding shares and interests in our pre-petition preferred stock and pre-petition common stock; and
- The issuance of approximately 95.0 million shares of new common stock in reorganized XO and warrants to purchase up to an additional 23.75 million shares of new common stock of reorganized XO.

The following table shows the distribution each party of interest impacted by XO Parent's bankruptcy was entitled to. As certain claims are still being reviewed by the Bankruptcy Court, certain proportional distributions have not yet been made and can not occur until the court rules (dollars in thousands, except share data).

Party of Interest	Shares of New Common Stock	Series A Warrants	Series B Warrants	Series C Warrants	Credit Facility	Cash
$1 Billion senior secured credit facility	90,250,001	—	—	—	$500,000	$ —
Senior unsecured notes	4,715,344	9,430,689	7,073,015	7,073,015	—	1,600
Subordinated notes	—	—	—	—	—	616
General unsecured creditors	34,656	69,309	51,980	51,980	—	403
Total entitlement	95,000,001	9,499,998	7,124,995	7,124,995	$500,000	$2,619
Not yet distributed	1,230,638	2,461,743	1,846,151	1,846,151	$ —	$1,612
Total issued or paid	93,769,363	7,038,255	5,278,844	5,278,844	$500,000	$1,007

See Notes 13 and 14 in Part IV for additional disclosure on our equity and debt instruments.

As part of our Plan of Reorganization, we agreed to initiate a Rights Offering that allowed certain holders of claims and interests in XO Parent as of the November 15, 2002 record date to subscribe for up to 40.0 million shares of New Common Stack at $5.00 per share. The Rights Offering closed on January 5, 2004. An aggregate of 39.7 million shares were issued, yielding net proceeds of $197.6 million. We used the proceeds from the Rights Offering to pay down our Credit Facility to $339.2 million in January 2004.

Interests Held by Entities Controlled by Mr. Carl C. Icahn

Various entities controlled by Mr. Icahn hold the following interests in reorganized XO:

	Common Stock	Series A, B and C Warrants	Credit Facility
At December 31, 2003	Greater than 80%	Greater than 40%	Greater than 90%
At January 31, 2004	Greater than 60%	Greater than 40%	Greater than 90%

In addition entities controlled by Mr. Icahn have acquired an option to purchase 6.25 million additional shares of common stock from Franklin Mutual Advisors, LLC at a strike price of $4.25 per share which expires June 21, 2004. After closing our rights offering in January 2004, Mr. Icahn's ownership interest in our outstanding common stock was reduced to over 60%.

As a result of this majority ownership position, Mr. Icahn can elect all of our directors, appoint the members of the committees of our Board of Directors, appoint key members of our executive management team, and appoint our auditors. Currently, Mr. Icahn is Chairman of the Board of Directors and three employees of Icahn Associates sit on our Board of Directors as well as various Committees of our Board of Directors. Under applicable law and our Certificate of Incorporation and by-laws, certain actions cannot be taken without the approval of holders of a majority of our voting stock, including, without limitation, mergers, acquisitions, the sale of substantially all our assets, and amendments to our Certificate of Incorporation and by-laws. We anticipate that Mr. Icahn will continue to control a majority of our outstanding capital stock following the issuance of XO Parent shares in connection with our acquisition of Allegiance assets and consequently will continue to have these governance rights.

Liquidity and Capital Resources

Capital Resources and Liquidity Assessment

Our operating, investing and financing activities during 2003 provided net cash of $6.3 million, $153.0 million and $5.2 million, respectively. Cash and cash equivalents increased to $478.6 million at December 31, 2003 from $314.0 million at December 31, 2002. However, our balance of cash and marketable securities decreased to $520.6 million at December 31, 2003 from $561.0 million at December 31, 2002. As discussed further in Item I, "Business", we expect that, in the near term, our business will use existing cash of approximately $311.0 million in cash and that we will issue approximately 45.4 million shares of our New Common Stock to acquire Allegiance's assets. In addition, we will use cash for capital expenditures and net working capital requirements. We expect that the majority of our planned capital expenditure requirements will be "success-based" in that they will be used to purchase and install customer-related equipment and electronics in connection with growing revenue by adding new customers or increasing the amount of services provided to existing customers. Much of the non-success based planned capital expenditures will be for the continued development and implementation of our information systems to support and enhance the provisioning and billing of new and existing customers in a more cost efficient manner. Part of our net working capital requirements are commitments under lease and contractual obligations for software licenses and ongoing support of software for IT and network applications and are disclosed in the table below.

There are no additional borrowings available under our Credit Facility. We raised net proceeds of $197.6 million in January 2004 upon the consummation of our Rights Offering, and applied these proceeds to the outstanding balance on the credit facility, reducing the amount outstanding from $536.8 million as of December 31, 2003 to $339.2 million. We have no current debt service requirements since cash interest payments as well as automatic and permanent quarterly reductions of the principal amount outstanding under the Credit Facility do not commence until 2009. However, in the event that consolidated excess cash flow (as defined in the Credit Facility) for any fiscal quarter during the term of the agreement is greater than $25 million, at the request of the lender, XO will pay an amount equal to 50% of such excess cash flow greater than $25 million toward the reduction of outstanding indebtedness. In addition, if the ratio of our consolidated earnings before interest, taxes depreciation and amortization for the four consecutive quarters exceeds 4:1, we would be required to pay cash interest, unless waived by the lenders.

The following table summarizes our payment obligations under various operating and financing agreements as of December 31, 2003 (dollars in thousands):

Year Ending December 31,	Credit Facility	Operating lease obligations	Other long-term contractual obligations	Capital lease obligations	Total obligations
2004	$ —	$ 60,623	$ 53,974	$2,809	$ 117,406
2005	—	57,974	33,768	2,668	94,410
2006	—	53,269	24,484	2,416	80,169
2007	—	49,159	23,451	1,733	74,343
2008	—	38,823	23,048	277	62,148
Thereafter	536,791	188,084	96,811	—	821,686
Total minimum commitments	$536,791	$447,932	$255,536	$9,903	$1,250,162

We used the proceeds from the Rights Offering to pay down our Credit Facility to $339.2 million in January 2004. As discussed in Part I, Item 1, Business, we lease wavelength capacity from Level 3 for intercity network capacity. The first of these leases expires in 2006. At that time, we will either renew these leased wavelengths or install our own optical equipment and light our intercity fiber network, either of which will be a substantial capital expenditure.

We expect that our current cash balance will be sufficient to fund our acquisition of Allegiance, net working capital and capital expenditure requirements and allow us to successfully execute our current business plan. However, if we are unsuccessful at integrating the assets acquired from Allegiance in a timely and/or cost effective manner, this expectation could be incorrect and cause us to issue additional equity and/or debt securities. Additionally, current economic conditions of the telecommunications industry may create opportunities for XO to bid on other companies or portions of companies at attractive prices. We expect to continue to pursue the acquisition of additional telecommunication companies or assets throughout 2004. We do not know what the terms of any such transactions would be. Any other offers involving cash consideration could significantly and adversely affect our liquidity. To support further business expansion, including investments in or acquisitions of other companies or portion of other companies, we may issue additional equity and/or debt securities.

Other 2003 Transactions and Developments

Announcement of Chief Executive Officer Appointment

On April 28, 2003, we announced that we had hired Carl J. Grivner as our new Chief Executive Officer effective May 15, 2003. Effective May 1, 2003, Mr. Grivner joined XO as a member of the newly created Office of the Chairman. Mr. Grivner's career in the telecommunications and technology industries spans more than 25 years. He most recently served as Chief Operating Officer of Global Crossing, Ltd. Prior to joining Global Crossing in June 2000, Mr. Grivner served as Chief Executive Officer of Worldport Communications and, before that, he served as Chief Executive Officer, Western Hemisphere, of Cable & Wireless PLC. Additionally, Mr. Grivner has held various senior executive positions at Advanced Fiber Communications and Ameritech.

Comparison of Financial Results

As a consequence of the Chapter 11 reorganization, the financial results for the year ended December 31, 2003 have been separately presented under the label "Reorganized XO" and are not comparable with prior year results. The reorganized Company has adopted the policy of expensing customer installation costs and internal labor directly associated with network construction in the period in which the costs are incurred. The predecessor Company capitalized and amortized these costs. In accordance with SOP 90-7, the reorganized Company was required to implement newly issued accounting pronouncements that would require adoption within twelve months of applying fresh start.

The operational results for the year ended December 31, 2003 are discussed below. The projected trends are for XO operations as we exit 2003, and do not include the impact of any revenue or cost synergies from the Allegiance acquisition, or any other acquisitions that might occur in 2004.

Reorganized XO Year Ended December 31, 2003 Compared to Predecessor XO Year Ended December 31, 2002

Revenue. Total revenue for the year ending December 31, 2003 decreased 11.8% to $1,110.5 million from $1,259.9 million for the year ending December 31, 2002. Customer churn, of approximately 2.4% in 2003, exceeded acquisition revenue particularly in the carrier, stand alone, DSL and dial-up customer base. The majority of this decline is driven by major reductions in the carrier revenue stream due to bankruptcies, downsizing network requirements, as well as competitive pricing pressures. Additionally, year-over-year revenue decreased in ancillary stand alone products such as Dial Up and DSL Internet access, and Hosting due to XO focusing on more profitable offerings. The commercial offerings to middle market businesses, however, remained relatively stable as revenue acquisition kept pace with attrition.

We anticipate that the negative trends within the carrier revenue stream will stabilize during the first half of 2004 as customer churn improved during 2003 from 2.6% during the first three quarters of 2003 to 1.9% during the fourth quarter of 2003. Therefore, XO estimates that the first half of 2004 revenue will be relatively consistent with the fourth quarter 2003 exit run rate. Additionally, we estimate that sequential year-over-year, 2003 revenue versus 2004, should remain relatively constant.

Revenue was earned from providing the following services (dollars in thousands):

	Reorganized XO		Predecessor XO		
	Year Ended December 31,		Year Ended December 31,		
	2003	% of 2003 Revenue	2002	% of 2002 Revenue	% Change
Voice services	$ 572,774	51.6%	$ 659,558	52.3%	(13.2%)
Data services	392,742	35.4%	472,247	37.5%	(16.8%)
Integrated voice and data services	144,967	13.0%	128,048	10.2%	13.2%
Total revenue	$1,110,483	100.0%	$1,259,853	100.0%	(11.8%)

Voice services revenue includes revenue from local and long distance voice services, prepaid calling card processing, and other voice telecommunications based services, interactive voice response services and stand-alone long distance services. Voice services revenue for the year ended December 31, 2003 decreased to $572.8 million from $659.6 million for the same period of 2002. The decrease is attributable to reduced FCC mandated rates, price reductions in long distance services due to reduced cost of service due to technological improvements, and customer disconnects and usage reductions arising from customers' downsizing due to the state of the domestic economy.

Data services revenue includes revenue from Internet access, network access and web applications hosting services. Data services revenue for the year ended December 31, 2003 decreased to $392.7 million from $472.2 million for the same period of 2002. The decline was attributable to an increase in customer bankruptcies, and customer disconnects, and a lower demand from large customers due to reductions in those customers' data capacity needs.

Integrated voice and data services revenue is generated largely from our XOptions service offerings, a flat-rate bundled package offering a combination of voice and data services. Integrated voice and data services revenue for the year ended December 31, 2003 increased to $145.0 million from $128.0 million for the same period in 2002. The increase is due to the continued acceptance in the marketplace of our XOptions service offering.

Costs and expenses. The table below provides costs and expenses by classification and as a percentage of revenue (dollars in thousands):

	Reorganized XO		Predecessor XO		
	Year Ended December 31,		Year Ended December 31,		
	2003	% of 2003 Revenue	2002	% of 2002 Revenue	% Change
Costs and expenses:					
Cost of service	$ 422,129	38.0%	$ 522,924	41.5%	(19.3%)
Selling, operating and general	679,286	61.2%	765,853	60.8%	(11.3%)
Depreciation and amortization	109,308	9.9%	699,806	55.5%	(84.4%)
Restructuring and asset write-downs	11,618	1.1%	480,168	38.1%	(97.6%)
Total	$1,222,341		$2,468,751		(50.5%)

Cost of service. Cost of service includes expenses directly associated with providing telecommunications services to our customers. Cost of service includes, among other items, the cost of connecting customers to our networks via leased facilities, the costs of leasing components of our network facilities and costs paid to third party service providers for interconnect access and transport services. Cost of service for the year ended December 31, 2003 decreased in absolute dollars and as a percentage of revenue compared to the same period in 2002. The year over year decline as a percentage of revenue was due primarily to cost optimization programs which reduced expenses by transferring traffic from third party facilities onto our owned or controlled facilities, and favorable resolutions of disputed third party costs. The decline was partially offset by our adoption of an accounting policy during the first quarter of 2003, to expense rather than defer costs associated with the installation of customer services and the revenue reductions in carrier long-distance services due to the excess long haul capacity in the sector.

We estimate that cost of service as a percentage of revenue will increase slightly when compared to 2003 results due to the loss of higher margin private line carrier revenue. It may also fluctuate quarter-to-quarter based on trends in revenue, product mix, the impact of customer bankruptcies, regulatory decisions and our ability to continue favorable resolution of third party billing disputes.

Selling, operating and general. Selling, operating and general expense includes expenses related to sales and marketing, internal network operations and engineering, information systems, general corporate office functions and collection risks. Selling, operating and general expense for the year ended December 31, 2003 was $679.3 million or 61.2% of revenue versus $765.9 million or 60.8% of revenue for the year ended December 31, 2002. Selling, operating and general expense decreased in absolute dollars due to our reorganization that resulted in reduced headcount, contract rejections and renegotiations, and fair value adjustments to our long term contractual commitments and property as required by fresh start accounting which resulted in expense reductions in various contracted services, rent and property taxes. These reductions were partially offset by our adoption of the policy of expensing internal labor costs directly associated with customer installation and the construction of our network. The increase in selling, operating and general expense as a percentage of revenue for the year ended December 31, 2003 when compared to 2002 results is due to the large reduction of revenues due to bankruptcies and price declines discussed above, with no associated offsetting direct expense reduction.

We expect selling, operating and general expense to decrease in absolute dollars and to remain relatively stable as a percentage of revenue in the near term. With the headcount reduction in early 2003 and management's focus on selling larger dollar, more profitable services, we are projecting that selling, operating, and general expenses as a percentage of revenue will decrease as a percentage or revenue in the second half of 2004. We further believe that the Allegiance acquisition will contribute to this trend.

Depreciation and amortization. As discussed above, we implemented fresh start on January 1, 2003 and adjusted the carrying value of our property and equipment and other intangibles to their fair value which resulted in a significant reduction of the aggregate historical carrying value. Consequently, depreciation and amortization expense decreased to $109.3 million for the year ended December 31, 2003, versus $699.8 million for the year ended December 31, 2002.

We expect depreciation and amortization expense during 2004 to increase slightly as additional assets are placed into service. As of December 31, 2003, we had approximately $80.0 million of construction-in-progress plus $23.5 million of broadband wireless licenses that have not yet been placed into service and, accordingly, are not currently being depreciated or amortized.

Restructuring and asset write-downs. Restructuring and asset write-downs decreased to $11.6 million for the year ended December 31, 2003 from $480.2 million for the year ended December 31, 2002. Restructuring charges in 2003 include costs for a reduction in our workforce by approximately 550 employees, primarily employed in network operations, sales and marketing and information technology and estimated losses associated with restructured leases.

The 2002 restructuring charges primarily include a $477.3 million non-cash asset write-down during the third quarter of 2002 as a result of returning intercity assets to Level 3 in exchange for reduced future maintenance expenses beginning in 2003.

Investment income (loss), net. Investment income (loss), net includes interest income as well as any realized gains or losses from the sale of investments. Investment income (loss), net was a gain of $46.2 million for 2003 and a gain of $16.3 million in 2002. The 2003 balance is primarily for a gain on the sale of an investment.

Interest expense, net. Interest expense, net includes interest expense on debt and capital leases, less any amounts capitalized for construction efforts. The majority of interest expense in 2003 is non-cash as the Credit Facility allows for accrued interest to be converted into principal if unpaid. Interest expense, net for the years ended December 31, 2003 and 2002 was $36.8 million and $226.5 million, respectively. During 2003 and 2002, XO capitalized interest on construction costs of $3.0 million and $11.1 million, respectively. Contractual interest was $501.1 million for the year ended December 31, 2002. The significant reduction for 2003 was caused by the cancellation of our pre-petition senior notes and pre-petition convertible subordinated notes and the reduction in the amount outstanding under our Credit Facility upon consummation of our Plan of Reorganization. We expect interest expense to decline further in 2004 due to the pay down of the Credit Facility with the proceeds of the Rights Offering in January 2004.

Predecessor XO Year Ended December 31, 2002 Compared to Predecessor XO Year Ended December 31, 2001

Revenue. Total revenue in 2002 of $1,259.9 million was consistent with total revenue in 2001 of $1,258.6 million. The weakened economy and the perceived uncertainties in the market regarding XO Parent's Chapter 11 proceedings had a negative impact on our ability to generate new sources of revenue. Consequently, we were not able to maintain the level of growth that we had historically achieved. We experienced a high level of customer disconnects in 2002 due to reduced demand from other telecommunications companies and increased customer bankruptcies in the telecommunications and dot-com industries.

Revenue was earned from providing the following services (dollars in thousands):

	Predecessor XO				
	Year Ended December 31,				
	2002	% of 2002 Revenue	2001	% of 2001 Revenue	% Change
Voice services	$ 659,558	52.3%	$ 609,885	48.4%	8.0%
Data services	472,247	37.5%	596,664	47.5%	(20.9%)
Integrated voice and data services	128,048	10.2%	52,018	4.1%	146.2%
Total revenue	$1,259,853	100.0%	$1,258,567	100.0%	0.1%

Voice services revenue includes revenue from bundled local and long distance voice services, prepaid calling card processing, and other voice communications based services, interactive voice response services and stand-alone long distance services. Voice services revenue in 2002 increased to $659.6 million from $609.9 million in 2001. The increase was primarily due to more sales to larger business customers, including the impact of the rollout of our carrier long distance service.

Data services revenue includes revenue from Internet access, network access and web applications hosting services. Data services revenue in 2002 decreased to $472.2 million from $596.7 million in 2001. This decline was attributable primarily to customer bankruptcies affecting some large network access customers, increased levels of customer disconnects, and a lower demand from large customers due to reductions in those customers' data and fiber capacity needs. The sale of our European operations in February 2002 also contributed to this decline.

Integrated voice and data services revenue is generated largely from our XOptions service offerings, a flat-rate bundled package offering a combination of voice and data services. Integrated voice and data services revenue in 2002 increased to $128.0 million from $52.0 million in 2001. The increase is primarily attributed to an increase in the number of customers to whom we provide X Options service.

Costs and expenses. The table below provides costs and expenses by classification and as a percentage of revenue (dollars in thousands):

	Predecessor XO				
	Year Ended December 31,				
	2002	% of 2002 Revenue	2001	% of 2001 Revenue	% Change
Costs and expenses:					
Cost of service	$ 522,924	41.5%	$ 527,698	41.9%	(0.9%)
Selling, operating and general	765,853	60.8%	1,008,887	80.2%	(24.2%)
Depreciation and amortization	699,806	55.5%	1,162,671	92.4%	(39.8%)
Restructuring and asset write-downs	480,168	38.1%	509,202	40.5%	(5.7%)
Total	$2,468,751		$3,208,458		(23.1%)

Cost of service. Cost of service includes expenses directly associated with providing telecommunications services to our customers. Cost of service includes, among other items, the cost of connecting customers to our networks via leased facilities, the costs of leasing components of our network facilities and costs paid to third party providers for interconnect access and transport services. Cost of service in 2002 was $522.9 million or 41.5% of revenue compared to $527.7 million or 41.9% of revenue in 2001. The 2002 decline was due primarily to cost optimization programs to reduce expenses by transferring traffic from leased facilities onto facilities owned or controlled by us. These cost reductions were offset, to some extent, by increased costs of service that were attributable to the increase in voice and integrated services revenue as a percentage of our total revenue. These revenues generally carry lower margins when compared to data services because voice and integrated services are more likely to utilize leased versus owned network facilities to terminate calls.

Selling, operating and general. Selling, operating and general expense includes expenses related to sales and marketing, internal network operations and engineering, information systems, general corporate office functions and expenses relating to collection risks. Selling, operating and general expense in 2002 was $765.9 million compared to $1,008.9 million in 2001. Selling, operating and general expense decreased both in absolute dollars and as a percentage of revenue in 2002 when compared to 2001 due to efficiencies resulting from the centralization of and process improvements in many functions and cost reduction and restructuring initiatives that included significant headcount reductions and savings from the planned exit of certain leased facilities, as well as the February 2002 sale of our European operations.

Depreciation and amortization. We have constructed an integrated facilities-based network in the United States. Primarily in late 2001 and early 2002, we expanded our services in existing markets, placed more assets into service, and increased our obsolescence expense, all of which caused depreciation expense to increase to $598.5 million in 2002 from $447.0 million in 2001. In 2003, in conjunction with our implementation of fresh start accounting, we adjusted the carrying value of our property and equipment to its estimated fair value of $502.2 million from a net carrying value of $2,780.6 million at December 31, 2002. Accordingly, depreciation expense has decreased significantly during 2003 and in future periods when compared to depreciation expense for periods prior to the effective date of the Plan of Reorganization.

Amortization expense includes the amortization of broadband wireless licenses and other intangibles assets with definite lives and, for 2001, also includes the amortization of goodwill. Amortization expense decreased to $101.3 million in 2002 from $715.7 million in 2001. The significant decrease is primarily due to our implementation of SFAS No. 142 and the resulting write-off of all our goodwill as of January 1, 2002. In conjunction with our implementation of fresh start accounting in 2003, we reduced the $911.8 million December 31, 2002 carrying value of our broadband wireless licenses to their estimated fair value of approximately $60.0 million, and increase the $72.8 million December 31, 2002 net carrying value of other intangible assets to their estimated fair value of approximately $76.0 million. Accordingly, amortization expense decreased in 2003 and in future periods when compared to amortization expense for periods prior to the effective date of the Plan of Reorganization.

As of December 31, 2002, our balance sheet reflected approximately $731.0 million of long-lived assets, including construction-in-progress and certain broadband wireless licenses that had not been placed into service and, accordingly, were not being depreciated or amortized. As discussed above, these long-lived assets were written down to their estimated fair values when we applied fresh start accounting during the first quarter of 2003.

Restructuring and asset write-downs. Restructuring and asset write-downs were $480.2 million in 2002 and $509.2 million in 2001. During 2001, restructuring charges primarily related to the implementation of our plan to restructure certain of our business operations. The restructuring plan included divesting certain assets and businesses, and reducing our discretionary spending, capital expenditures and workforce, based on our assessment of current and future market conditions. The 2001 restructuring charges include a $366.8 million write-down for the excess of carrying value of assets to be sold or abandoned, including our European business unit, and a $134.4 million restructuring charge relating to the consolidation and exiting of domestic facility leases, which was determined based on the future minimum rent commitments for the buildings that management intended to exit less estimated sublease rental streams. The 2001 restructuring charges also included an $8.0 million restructuring charge related to involuntary termination severance costs with respect to 700 persons whose employment was terminated in connection with a workforce reduction, the majority of whom were terminated by December 31, 2001.

During 2002, we continued to restructure our operations and reduced our workforce by approximately 350 additional employees, the majority of whom were employed in network operations, sales and marketing and information technology, and recorded a $2.9 million restructuring charge related to the involuntary termination severance costs. In addition, we recorded a $477.3 million non-cash asset write-down during the third quarter of 2002 as a result of returning intercity assets to Level 3 in exchange for reduced future maintenance expenses beginning in 2003.

Investment income (loss), net. Investment income (loss), net in 2002 was net income of $16.3 million versus a net loss of $15.8 million in 2001. Investment income, net is mostly interest income in 2002 while the 2001 net (loss) includes an $89.0 million write down for an other than temporary decline in the value of certain investments.

Interest expense, net. Interest expense, net in 2002 decreased to $226.5 million from $465.4 million in 2001, as we ceased accruing interest and penalties on our pre-petition senior unsecured, subordinated notes and Pre-Petition Facility as of the petition date, in accordance with SOP 90-7. The contractual interest amounts of $501.1 million reflected on the consolidated statement of operations represents the interest expense that would have been accrued under the relevant financing agreements had we not ceased accruing interest as described above.

Gain on repurchase of debt. Gain on repurchase of debt in 2001 was $345.0 million related to our repurchase of $557.1 million of senior notes at a substantial discount from their respective face values.

Reorganization gain (expense), net. Reorganization gain, net of $3,032.3 million at January 1, 2003 include gains from our debt and preferred stock cancellations upon our emergence from bankruptcy less the loss recorded in adjusting our long-term assets and liabilities to fair value upon our application of the fresh start accounting required by SOP 90-7. Reorganization expense in 2002 was $91.1 million and included the (i) non-cash charges relating to the write off of issuance costs, discounts and purchase accounting adjustments to adjust the historical carrying amounts of our debt to the allowed claim amount by the Bankruptcy Court, (ii) professional fees associated with our Plan of Reorganization, (iii) the penalties from the rejection of contracts, (iv) adjustments to unpaid pre-petition accounts payable and accrued expenses to the claim amounts allowed by the bankruptcy court, and (v) the net gain resulting from payments received by XO Parent in connection with the settlement and termination of the proposed investment transaction that was the basis for the first restructuring alternative contemplated by the Plan of Reorganization, less amounts paid to settle certain stockholder claims.

Cumulative effect of accounting change. We performed the transitional impairment tests of goodwill as required by SFAS No. 142 as of January 1, 2002. Based on these tests, we recorded a $1,876.6 million impairment charge to write-off all of our goodwill as a cumulative effect of accounting change during the first quarter of 2002.

Recognition of preferred stock modification fee, net — reorganization item. In order to adjust the historical carrying amount of our preferred stock to the amount allowed by the Bankruptcy Court, we recognized the unamortized balance of a deferred modification fee with respect to our preferred stock as of the petition date and wrote off certain unamortized issuance costs and recognized certain purchase accounting adjustments related to the preferred stock which netted a $78.7 million gain during 2002.

Gain on repurchases of preferred stock, net. In 2001, we recorded a net gain totaling $376.9 million related to our repurchase of $472.6 million in liquidation preference of our preferred stock at a substantial discount from the respective carrying amounts.

Preferred stock dividends and accretion of preferred stock redemption obligation, net. As our preferred stock was deemed subject to compromise under SOP 90-7, we ceased accruing dividends and accreting the redemption obligation on all of our outstanding preferred stock as of our petition date. As a result, we recorded $42.2 million of preferred stock dividends during 2002 as compared to $129.7 million in such dividends in 2001. The contractual dividend amount of $98.8 million reflected on the accompanying consolidated statement of operations represents the dividends that would have been accrued under the terms of our preferred stock had we not ceased accruing such dividends as described above.

Critical Accounting Policies and Estimates

As of January 1, 2003, we adopted the policy of expensing customer installation costs and internal labor directly associated with network construction in the period in which the costs are incurred as this labor effort is not specific to any large segregated project, but rather to ordinary course business operations. During 2002 we capitalized and amortized these costs. During 2002, the net decrease to cost of sales and to selling, operating and general expenses as a result of capitalization and amortizing these costs was approximately $14.3 million and $9.5 million, respectively.

The preparation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States requires management to make judgments, estimates and assumptions regarding uncertainties that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. Management uses historical experience and all available information to make these judgments and estimates and actual results could differ from those estimates and assumptions that are used to prepare our financial statements at any given time. Despite these inherent limitations, management believes that Management's Discussion and Analysis and the accompanying consolidated financial statements and footnotes provide a meaningful and fair perspective of our financial condition and our operating results for the current period. Management believes the following critical accounting policies represent the more significant judgments and estimates used in the preparation of our audited consolidated financial statements included in this form 10-K.

Fresh-Start Adjustments

Fresh start required that XO adjust the historical cost of its assets and liabilities to their fair values as determined by the reorganization value of the Company. Fresh start requires that the reorganization value be allocated to the entity's net assets in conformity with procedures specified by SFAS No. 141, "Business Combinations," ("SFAS No. 141"). We engaged an independent appraiser to assist in the allocation of the reorganization value to the reorganized Company's assets and liabilities by determining the fair market value of its property and equipment, intangible assets and certain obligations related to its facility leases. Many estimates, projections and assumptions are used to assess the fair value of long term assets and liabilities. We review these estimates quarterly to determine if actual results are consistent with our assumptions. Any adjustments are recorded in the quarterly results. The accounting impact from adopting fresh start is included in Part II, Item 6, Selected Financial Data.

Long-Lived Assets

Our long-lived assets include property and equipment, broadband wireless licenses, and identifiable intangible assets to be held and used. The estimated useful lives of telecommunications networks and acquired bandwidth are 3 to 20 years and 5 to 7 years for furniture fixtures, equipment and other. These useful lives are determined based on historical usage with consideration given to technological changes and trends in the industry that could impact the network architecture and asset utilization. This latter assessment is significant because we operate within an industry in which new technological changes could render some or all of our network related equipment obsolete requiring application of a shorter useful life or, in certain circumstances, a write-off of the entire value of the asset. Accordingly, in making this assessment, we consider our planned use of the assets, the views of experts both from internal and outside sources regarding the impact of technological advances and trends in the industry on the value and useful lives of our network assets.

Investments in broadband wireless licenses acquired prior to December 31, 2002 were recorded at their fair values at January 1, 2003, as required by fresh start. We are amortizing these over the license period of 10 years as determined by the Federal Communications Commission. In order to receive an extension on the original license term from the FCC, we are required to show substantial service in the license area within ten years of being licensed. Failure to meet this requirement could result in forfeiture of the license. Approximately $23.5 million in book value of these licenses have not yet been placed into service. Had these licenses been in service during all of 2003, amortization expense would have increased by approximately $4.4 million. If we fail to show substantial service in the licensed geographic area at the end of the original ten year period and fail to negotiate an extension from the FCC, we would forfeit the right to offer such services in that market, and write-off the impaired asset. XO is evaluating recent improvements in the price and performance of broadband wireless equipment, and is developing a plan to meet the FCC's substantial service test in all its licensed areas before the licenses are due for renewal proceedings.

Revenue Recognition

Revenues from telecommunications services are recognized when the services are performed, evidence of an arrangement exists, the fee is fixed and determinable and collectibility is probable. In circumstances when these criteria are not met, revenue recognition is deferred until resolution occurs. For example, if a customer files for protection under bankruptcy, we believe the probability of collection is weakened. Consequently, under such circumstances, although we continue to bill the customer for all services provided, we do not recognize revenue until cash is received. In addition, telecommunications customers often dispute the amounts that we invoice them due to regulatory issues, late payment fees, and early termination charges based on differences of opinion regarding contract terms or service levels. Accordingly, as these billings are not considered fixed and determinable and collection of such amounts is not considered probable while these amounts are disputed, revenue recognition is deferred until the dispute is resolved and the cash is collected.

Service discounts and incentives related to telecommunications services are recorded as a reduction of revenue when granted or ratably over a contract period. Fees billed in connection with customer installations and other non-recurring fees are deferred and recognized ratably over the estimated customer life. The estimated customer life is calculated by analyzing customer disconnects as a percentage of revenue. This calculation is reviewed every quarter.

We establish an allowance for collection of doubtful accounts and other sales credit adjustments. Allowances for sales credits are established through a charge to revenue, while allowances for doubtful accounts are established through a charge to selling, operating and general expenses. We assess the adequacy of these reserves monthly by considering general factors, such as the length of time individual receivables are past due, historical collection experience, the economic and competitive environment, and changes in the credit worthiness of our customers. As considered necessary, we also assess the ability of specific customers to meet their financial obligations to us and establish specific valuation allowances based on the amount we expect to collect from these customers. We can and have experienced material changes to our reserve requirements on a month to month basis as significant customers have in the past unexpectedly filed for bankruptcy or otherwise became insolvent. We believe that our established valuation allowances were adequate as of December 31, 2003. If circumstances relating to specific customers change or economic conditions worsen such that our past collection experience and assessment of the economic environment are no longer valid, our estimate of the recoverability of our trade receivables could be changed. If this occurs, we would adjust our valuation allowance in the period the new information is known.

Cost of Service

Cost of service includes expenses directly associated with providing telecommunications services to customers, including, among other items, the cost of connecting customers to our networks via leased facilities, the costs of leasing components of our network facilities and costs paid to third party providers for local access and transport services. All such costs are expensed as incurred. We accrue for the expected costs of services received from third party telecommunications providers during the period the services are rendered. Invoices received from the third party telecommunications providers are often disputed due to billing discrepancies. We accrue for all invoiced amounts, even amounts in dispute, as these amounts represent contingent liabilities that are considered probable and measurable. Disputes resolved in our favor may reduce cost of service in the period the dispute is settled and typically reflect costs paid in prior periods. Because the period of time required to resolve these types of disputes often lapses over several quarters, the benefits associated with the favorable resolution of such disputes normally are realized in periods subsequent to the accrual of the disputed invoice.

Off-Balance Sheet Arrangements

We are not currently engaged in the use of off-balance sheet derivative financial instruments, to hedge or partially hedge interest rate exposure nor do we maintain any other off-balance sheet arrangements for the purpose of credit enhancement, hedging transactions, or other financial or investment purposes.

Recent Accounting Pronouncements Implemented in 2003

In June 2001, the Financial Accounting Standards Board, issued SFAS No. 143, "Accounting for Asset Retirement Obligations," ("SFAS No. 143"), which requires an entity to recognize the fair value of a liability for an asset retirement obligation in the period in which a legal or contractual removal obligation is incurred if a reasonable estimate of fair value can be made. If a reasonable estimate of fair value cannot be made in the period the asset retirement obligation is incurred, SFAS No. 143 requires the liability to be recognized when a reasonable estimate of the fair value can be made. As required by SOP 90-7, we implemented SFAS No. 143 on January 1, 2003, in conjunction with the implementation of fresh start and recorded an estimated asset retirement obligation of $12.0 million.

Effective January 1, 2003, we adopted SFAS No. 145, "Rescission of the Financial Accounting Standards Board Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections as of April 2002", which eliminates the requirement to report material gains or losses from debt extinguishments as an extraordinary item, net of any applicable income tax effect, in an entity's statement of operations. SFAS No. 145 instead requires that a gain or loss recognized from a debt extinguishment be classified as an extraordinary item only when the extinguishment meets the criteria of both "unusual in nature" and "infrequent in occurrence" as prescribed under APB Opinion No. 30, "Reporting the Results of Operations — Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions". Upon adopting SFAS No. 145, the Company reclassified a 2001 $345.0 million gain from debt repurchases from extraordinary to recurring.

Effective January 1, 2003, the Company adopted SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities", which requires that costs, including severance costs, associated with exit or disposal activities be recorded at their fair value when a liability has been incurred. Under previous guidance, certain exit costs, including severance costs, were accrued upon managements' commitment to an exit plan, which is generally before an actual liability has been incurred. The adoption of SFAS No. 146 did not have a material effect on the Company's consolidated financial statements.

In December 2002, the FASB issued SFAS No. 148, which amends SFAS No. 123, to provide alternative methods of transition to SFAS No. 123's fair value method of accounting for stock-based employee compensation. As discussed and disclosed in Note 5, SFAS No. 148 also amends the disclosure provisions of SFAS No. 123 and APB No. 28. As allowed by SFAS No. 148, we have chosen to continue to account for compensation cost associated with our employee stock plans in accordance with the intrinsic value method prescribed by APB No. 25.

In May 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities,", which amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133. SFAS No. 149 is effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. The adoption of SFAS No. 149 did not have a material impact on the Company's consolidated financial statements.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity,", which establishes standards for how companies classify and measure certain financial instruments with characteristics of both liabilities and equity. It requires companies to classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). SFAS No. 150 is effective beginning with the second quarter of fiscal 2003. The adoption of SFAS No. 150 did not have a material impact on the Company's consolidated financial statements.

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities," an interpretation of Accounting Research Bulletin No. 51, "Consolidated Financial Statements" ("FIN 46"). FIN 46 applies to any business enterprise that has a controlling interest, contractual relationship or other business relationship with a variable interest entity ("VIE") and establishes guidance for the consolidation of VIEs that function to support the activities of the primary beneficiary. In December 2003, the FASB completed its deliberations regarding the proposed modification to FIN 46 and issued Interpretation Number 46R, "Consolidation of Variable Interest Entities-an Interpretation of ARB No. 51". The decision reached included a deferral of the effective date and provisions for additional scope exception for certain type of variable interests. Application of FIN 46R is required in financial statements of public entities that have interests in VIEs or potential VIEs commonly referred to as special-purpose entities for period ending after December 15, 2003. Application by public entities (other than small business issuers) for all other types of entities is required in financial statements for periods ending after March 15, 2004. The Company does not believe that the adoption of FIN 46R will have any effect on the Company's consolidated financial statements.

In November 2002, the FASB's Emerging Issues Task Force reached a final consensus on Issue No. 00-21. "Accounting for Revenue arrangements with Multiple Deliverables", which is effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. Under the EITF 00-21, revenue arrangements with multiple deliverables are required to be divided into separate units of accounting under certain circumstances. The adoption of EITF 00-21 did not have a material effect on the Company's consolidated financial statements.

In December 2003, the SEC issued Staff Accounting Bulletin No. 104, "Revenue Recognition", which updates the guidance in SAB No. 101, integrates the related set of Frequently Asked Questions, and recognizes the role of EITF 00-21. The adoption of SAB No. 104 did not have a material effect on the Company's consolidated financial statements.

Item 7A. Quantitative and Qualitative Disclosure About Market Risk

As of December 31, 2003, our Credit Facility was comprised of $529.9 million in secured loans and $6.9 million of accrued interest. We raised net proceeds of $197.6 million in January 2004, and applied these proceeds to the outstanding balance of the Credit Facility, reducing the total amount outstanding from $536.8 million to $339.2 million. Currently, we do not pay cash interest on the Credit Facility and accrued interest converts to principal ratably throughout the loan period. As interest accrues at variable rates, our Credit Facility subjects us to interest rate risks. Interest rate risk as of December 31, 2003 is illustrated in the following table (dollars in millions).

	Annual Interest Expense Given an Interest Rate decrease of X Basis Points			No Change in Interest Rates	Annual Interest Expense Given an Interest Rate increase of X Basis Points		
Interest Rate Risk	(150 BPS)	(100 BPS)	(50 BPS)	Fair Value	50 BPS	100 BPS	150 BPS
Credit Facility	$20.6	$22.3	$24.0	$25.7	$27.4	$29.1	$30.8

The sensitivity analysis provides only a limited, point in time view of the market risk sensitivity of the loans under our Credit Facility. The actual impact of market interest rate changes may differ significantly from those shown in the above sensitivity analysis.

Marketable securities, available for sale, at December 31, 2003 consist primarily of investments in equity and debt securities of publicly traded companies. The fair value of our investment in equity and debt securities exposes us to market risk. These investments are subject to changes in the market price of the securities. The table that follows summarizes the fair values of our marketable securities and provides a sensitivity analysis of the estimated fair value of these financial instruments assuming a 5%, 10% and 15% increase or decrease in market price (dollars in millions).

	Fair value assuming the following percentage increase in equity price			No Change in Fair Value	Fair value assuming the following percentage decrease in equity price		
Market Risk	15%	10%	5%	0%	5%	10%	15%
Market price	$35.8	$37.9	$40.0	$42.1	$44.2	$46.3	$48.4

Item 8. Financial Statements and Supplementary Data

Our consolidated financial statements are filed under this Item, beginning on page F-1 of this Report.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

On September 24, 2003, we notified our independent auditors, Ernst & Young LLP that our Audit Committee of our Board of Directors had decided to change auditors. On September 30, 2003, the Audit Committee of XO's Board of Directors appointed KPMG LLP to serve as its new independent auditors for the year ending December 31, 2003. The change was effective immediately. Ernst & Young LLP's report on XO's consolidated financial statements as of and for the year ended December 31, 2002 did not contain an adverse opinion or disclaimer of opinion, nor was it qualified or modified as to uncertainty, audit scope or accounting principles. During the fiscal year ending December 31, 2002, there were: (i) no disagreements with Ernst & Young on any matter of accounting principle or practice, financial statement disclosure or auditing scope or procedure which, if not resolved to Ernst & Young's satisfaction, would have caused them to make reference to the subject matter in connection with their report on our financial statements for such years; and (ii) there were no reportable events as defined in Item 304(a)(1)(v) of Regulation S-K.

During each of the years ended December 31, 2002 and December 31, 2001 and through the date of their appointment, we did not consult KPMG LLP with respect to the application of accounting principles to a specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on our consolidated financial statements, or any other matters or reportable events listed in Items 304(a)(2)(i) and (ii) of Regulation S-K.

On May 15, 2002, we dismissed our independent auditors, Arthur Andersen LLP, and appointed Ernst & Young LLP to serve as our new independent auditors for the year ending December 31, 2002. Our Board of Directors approved this decision. We filed a current report on Form 8-K with the Commission on May 16, 2002, which included a notification that the change was effective on May 15, 2002. Arthur Andersen's report on the Company's financial statements for the fiscal year ending December 31, 2001 included an explanatory paragraph that discussed the substantial doubt concerning our ability to continue as a going concern. During the fiscal year ending December 31, 2001, there were: (i) no disagreements with Arthur Andersen on any matter of accounting principle or practice, financial statement disclosure or auditing scope or procedure which, if not resolved to Arthur Andersen's satisfaction, would have caused them to make reference to the subject matter in connection with their report on our financial statements for such years; and (ii) there were no reportable events as defined in Item 304(a)(1)(v) of Regulation S-K.

During the year ending December 31, 2001 and through the date of their appointment, we did not consult Ernst & Young with respect to the application of accounting principles to a specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on our financial statements, or any other matters or reportable events as set forth in Items 304(a)(2)(i) and (ii) of Regulation S-K.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The term disclosure controls and procedures is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934. These rules refer to the controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within required time periods. Our Principal Executive Officer and our Principal Financial Officer have evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on the evaluation they have concluded that, as of the end of such period the controls and procedures were effective at ensuring that required information was disclosed on a timely basis in our report filed under the Exchange Act.

Changes in Internal Controls over Financial Reporting

We maintain a system of internal accounting controls that are designed to provide reasonable assurance that our books and records accurately reflect our transactions and that our established policies and procedures are followed. For the year ended December 31, 2003, there were no changes to our internal controls or in other factors that could significantly affect our internal controls over financial reporting.

PART III

Item 10. Directors and Executive Officers of the Registrant

The information required by this Item is incorporated by reference from our definitive proxy statement for the 2004 Annual Meeting of Stockholders to be held on May 27, 2004 to be filed with the SEC pursuant to Regulation 14A within 120 days after the end of our 2003 fiscal year.

Code of Ethics

We have adopted a Code of Ethics within the meaning of Item 406(b) of Regulation S-K. This Code of Ethics applies to our principal executive officer, our principal financial officer and principal accounting officer, as well as all other employees. This Code of Ethics is publicly available on our website at www.xo.com. If we make substantive amendments to this Code of Ethics or grant any waiver, including any implicit waiver, we will disclose the nature of such amendment or waiver on our website or in a report on Form 8-K within five days of such amendment or waiver.

Audit Committee Financial Expert

Our Board of Directors has determined Vincent J. Intrieri is an "audit committee financial expert" as defined under Item 401(h) of Regulation S-K. The Board of Directors has based its determination on the fact the Mr. Intrieri is a certified public accountant, and was a partner at the Arthur Andersen accounting firm.

Item 11. Executive Compensation

The information required by this Item is incorporated by reference from the information provided under the heading "Executive Compensation" of our Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management

Information required by this Item with respect to Securities Authorized for Issuance under Equity Compensation Plans is incorporated herein by reference from the information provided in the proposal to approve the amendment of our Directors' Stock Option Plan under the heading "Equity Compensation Plan" of our Proxy Statement.

Information required by this Item with respect to Stock Ownership of Certain Beneficial Owners and Management is incorporated herein by reference from the information provided under the heading "Stock Ownership of Certain Beneficial Owners and Management" of our Proxy Statement.

Item 13. Certain Relationships and Related Transactions

Various entities controlled by Mr. Icahn hold the following interests in XO:

	Outstanding Common Stock	Series A, B and C Warrants	Credit Facility
At December 31, 2003	Greater than 80%	Greater than 40%	Greater than 90%
At January 31, 2004	Greater than 60%	Greater than 40%	Greater than 90%

In addition, entities controlled by Mr. Icahn have acquired an option to purchase 6.25 million additional shares of our common stock from Franklin Mutual Advisors, LLC at a strike price of $4.25 per share which expires June 21, 2004. After closing the Rights Offering in January 2004, Mr. Icahn's ownership interest in our outstanding common stock was reduced to over 60%.

As a result of his majority ownership, Mr. Icahn can elect all of our directors, appoint the members of the committees of our Board of Directors, appoint key members of our executive management team, and appoint our auditors. Currently, Mr. Icahn is Chairman of our Board of Directors and three employees of Icahn Associates sit on our Board of Directors and various Committees of the Board of Directors. Under applicable law and our Certificate of Incorporation and by-laws, certain action cannot be taken without the approval of holders of a majority of our voting stock, including, without limitation, mergers, acquisitions, the sale of substantially all our assets, and amendments to our Certificate of Incorporation and by-laws.

Mr. Icahn, through various entities that he owns or controls, has the right to require us to register, under the Securities Act of 1933, shares of New Common Stock held by such entities and to include shares of our New Common Stock held by them in certain registration statements filed by us, pursuant to a Registration Rights Agreement approved by the Bankruptcy Court in connection with XO Parent's Chapter 11 proceedings.

In February 2003, Dixon Properties, LLC ("Dixon"), which is controlled by Mr. Icahn, acquired ownership of the building in which our headquarters is located in a transaction that was approved by the Bankruptcy Court. We currently lease approximately 170,000 square feet of space in that building.

Pursuant to the assumed lease agreement, we have paid $3.3 million in lease expense to Dixon for the year ended December 31, 2003 and we are obligated to pay approximately $15.6 million to Dixon through the expiration of the initial term of the lease, which is November 30, 2007.

We have entered into a Tax Allocation Agreement, dated January 16, 2003, between us and Starfire Holding Corporation, the parent entity of the affiliated group of corporations controlled by Mr. Icahn. We and Starfire intend to file consolidated returns during the period in which Mr. Icahn's ownership of XO is equal to or greater than 80%, as required by the Internal Revenue Code. The Tax Allocation Agreement provides that Starfire will pay all consolidated federal income taxes on behalf of the Icahn consolidated group that includes us, and we will make payments to Starfire in an amount equal to the tax liability, if any, that it would have incurred if it were to file its own consolidated return separate and apart from Starfire. Upon the closing of the Rights Offering in January 2004, Mr. Icahn's ownership percentage fell below 80%. Consequently we will no longer file as part of Icahn's consolidated group after January 2004. Upon deconsolidation, the Tax Allocation Agreement generally provides that Starfire will reimburse us each year going forward for the excess of our actual income tax expense over the income tax that would have been owed if the net operating losses or other tax attributes used in prior periods by the Starfire consolidated group excluding us, if any, were still available to us.

The Company provides certain telecommunications services to companies affiliated with Mr. Icahn. For the year ended December 31, 2003, the total revenue recognized on such services affiliated with Mr. Icahn was approximately $0.4 million. We have purchased approximately $0.3 million in services from Icahn affiliates during 2003. During 2003, we purchased approximately $1.1 million in hardware and services from Dell Computers, Inc. Mr. Adam Dell, an XO director, is Mr. Michael Dell's, the Chief Executive Officer of Dell Computers, brother.

Item 14. Principal Accounting Fees and Services

Information with respect to fees paid to our principal accountant and our audit committee's pre-approval policies and procedures are incorporated herein by reference to the Proxy Statement to be filed pursuant to Regulation 14A.

PART IV

Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

(a) (1) and (2) Financial Statements and Schedule:

XO Communications, Inc.

(3) List of Exhibits — Refer to Exhibit Index, which is incorporated herein by reference.

(b) Reports on Form 8-K:

1. On October 7, 2003. XO filed a Current Report on Form 8-K disclosing the announcement by XO of preliminary financial results for the third quarter of 2003.

2. On October 16, 2003, XO filed a Current Report on Form 8-K disclosing the announcement by XO that XO commenced as of such date the first stage of a two stage rights offering of between 40,000,000 and 43,333,333 shares of XO common stock pursuant to XO's Chapter 11 reorganization that was confirmed by the Bankruptcy Court on November 15, 2002.

3. On November 19, 2003, XO filed a Current Report on Form 8-K disclosing the announcement by XO that XO received approximately $162.5 million in paid subscriptions for approximately 32.5 million shares of its common stock in the initial stage of its rights offering that concluded on November 14, 2003.

4. On November 25, 2003, XO filed a Current Report on Form 8-K disclosing the correction of certain erroneous administrative entries recorded by an external service provider in connection with XO's rights offering.

5. On December 8, 2003, XO filed a Current Report on Form 8-K disclosing the announcement by XO that it commenced the second stage of its rights offering as of such date in which XO would offer rights to purchase approximately 7.8 million shares of its new common stock.

6. On December 16, 2003, XO filed a Current Report on Form 8-K disclosing the announcement by XO that it received $192.0 million in value, consisting of $164.8 million in cash and $27.2 million of Global Crossing common stock (based on the closing price of $33 per share of Global Crossing common stock as of December 12, 2003), in exchange for the $158.5 million XO Communications paid to acquire approximately 34% of pre-petition senior debt of Global Crossing.

SIGNATURES

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

XO Communications, Inc.

Date: March 15, 2004

By: /s/ CARL J. GRIVNER

Carl J. Grivner
President and Chief Executive Officer
(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on March 15, 2004 by the following persons on behalf of the Registrant and in the capacities indicated:

Name	Title
/s/ CARL J. GRIVNER Carl J. Grivner	President and Chief Executive Officer (Principal Executive Officer)
/s/ WAYNE M. REHBERGER Wayne M. Rehberger	Executive Vice President and Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)
/s/ CARL C. ICAHN Carl C. Icahn	Chairman of the Board of Directors
/s/ ANDREW R. COHEN Andrew R. Cohen	Director
/s/ ADAM DELL Adam Dell	Director
/s/ VINCENT J. INTRIERI Vincent J. Intrieri	Director
/s/ KEITH MEISTER Keith Meister	Director

EXHIBIT INDEX

2.1 Third Amended Plan of Reorganization of XO Communications, Inc., dated July 22, 2002, (Incorporated herein by reference to exhibit 2.1 filed with the Current Report on Form 8-K/A of XO Communications, Inc., filed on November 26, 2002).

2.2 Plan Supplement, dated October 23, 2003, to the Third Amended Plan of Reorganization of XO Communications, Inc., dated July 22, 2002 (Incorporated herein by reference to exhibit 2.2 filed with the Current Report on Form 8-K/A of XO Communications, Inc., filed on November 26, 2002).

2.3 Order Confirming Third Amended Plan of Reorganization, dated November 15, 2002 (Incorporated herein by reference to exhibit 99.1 filed with the Current Report on Form 8-K/A of XO Communications, Inc., filed on November 26, 2002).

2.4 Asset Purchase Agreement, dated as of February 18, 2004, by and among XO Communications, Inc., Allegiance Telecom, Inc., and Allegiance Telecom Company Worldwide (Incorporated herein by reference to exhibit 10.1 filed with the Current Report on Form 8-K of XO Communications, Inc. filed on February 24, 2004).

2.5 Amended and Restated Certificate of Incorporation of XO Communications, Inc. (Incorporated herein by reference to exhibit 3.1 filed with the Registration Statement on Form 8-A of XO Communications, Inc., filed on February 7, 2003, pursuant to the Securities Exchange Act).

3.1 Amended and Restated Bylaws of XO Communications, Inc.

4.1 Form of Stock Certificate of New Common Stock (Incorporated herein by reference to exhibit 4.1 filed with the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003).

4.2 Series A Warrant Agreement, dated as of January 16, 2003, by and between XO Communications, Inc. and American Stock Transfer & Trust Company (Incorporated herein by reference to exhibit 10.1 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).

4.3 Series B Warrant Agreement, dated as of January 16, 2003, by and between XO Communications, Inc. and American Stock Transfer & Trust Company (Incorporated herein by reference to exhibit 10.2 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).

4.4 Series C Warrant Agreement, dated as of January 16, 2003, by and between XO Communications, Inc. and American Stock Transfer & Trust Company (Incorporated herein by reference to exhibit 10.3 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).

10.1 XO Communications, Inc. 2002 Stock Incentive Plan (Incorporated herein by reference to exhibit 10.1.1 to the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003).

10.2 XO Communications, Inc. Retention Bonus and Incentive Plan (Incorporated herein by reference to exhibit 10.1.2 to the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003).

10.3 Registration Rights Agreement, dated as of January 16, 2003, between XO Communications, Inc. and High River Limited Partnership and Meadow Walk Limited Partnership (Incorporated herein by reference to exhibit 10.4 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).

10.4 Tax Allocation Agreement, dated as of January 16, 2003, between XO Communications, Inc. and Starfire Holding Corporation (Incorporated herein by reference to exhibit 10.5 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).

10.5 Employment Term Sheet, dated as of April 30, 2003, delivered by XO Communications, Inc. to Carl J. Grivner, President and Chief Executive Officer of XO Communications, Inc. (Incorporated herein by reference to exhibit 10.1 filed with the Quarterly Report on Form 10-Q of XO Communications, Inc. for the three months ended March 31, 2003, filed on May 15, 2003).

10.6 Change in Control Agreement by and between XO Communications, Inc. and Carl J. Grivner, President and Chief Executive Officer of XO Communications, Inc. (Incorporated herein by reference to exhibit 10.2 filed with the Quarterly Report on Form 10-Q of XO Communications, Inc. for the three months ended March 31, 2003, filed on May 15, 2003).

10.7 Employment Agreement, dated as of January 3, 2000, by and between Nathaniel A. Davis and NEXTLINK Communications, Inc. (predecessor to XO Communications, Inc.) (Incorporated herein by reference to exhibit 10.11 filed with the Annual Report on Form 10-K of NEXTLINK Communications, Inc. and NEXTLINK Capital, Inc., for the year ended December 31, 1999, filed on March 30, 2000.)

10.8 Employment Agreement by and between John Jacquay and XO Communications, Inc. dated as of November 20, 2002.

10.9 Employment Agreement, dated as of November 20, 1999, by and between Gary Begeman and XO Communications, Inc.

10.10 Employment Agreement, effective as of September 25, 2000, by and between Wayne M. Rehberger and XO Communications, Inc.

10.11 Cost Sharing and IRU Agreement, dated July 18, 1998, between Level 3 Communications, LLC and XO Intercity Holdings No. 2, LLC (f/k/a INTERNEXT LLC) (Incorporated herein by reference to exhibit 10.8 filed with the quarterly report on Form 10-Q for the quarterly period ended September 30, 1998 of NEXTLINK Communications, Inc. and NEXTLINK Capital, Inc., filed on November 16, 1998).

10.12 Master Agreement, dated August 8, 2002, between Level 3 Communications, Inc. and XO Communications, Inc. (Incorporated herein by reference to exhibit 10.4.2 filed with the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003).

10.13 Amended and Restated Credit and Guaranty Agreement, dated as of January 16, 2003, among XO Communications, Inc., certain subsidiaries of XO Communications, Inc., the Lenders party thereto from time to time, and Mizuho Corporate Bank, as Administrative Agent (Incorporated herein by reference to exhibit 10.5 filed with the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003).

14.1 XO Communications, Inc. Code of Ethics

16.1.1 Letter from Arthur Andersen LLP to the Securities and Exchange Commission, dated May 15, 2002 (Incorporated herein by reference to exhibit 16 filed with the Current Report on Form 8-K of XO Communications Inc. filed on May 16, 2002).

21.1 Subsidiaries of XO Communications, Inc.

23.1 Consent of KPMG LLP

23.2 Consent of Ernst & Young LLP

23.3 Notice Regarding Lack of Consent of Arthur Andersen

31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.

31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.

32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

REPORT OF KPMG LLP, INDEPENDENT AUDITORS

The Board of Directors and Stockholders
XO Communications, Inc.:

We have audited the accompanying consolidated balance sheet of XO Communications, Inc. and subsidiaries as of December 31, 2003 (Reorganized XO), and the related consolidated statements of operations, stockholders' equity and cash flows for the periods from January 1, 2003 to December 31, 2003 (Reorganized XO period) and for the portion of January 1, 2003, related to the Predecessor's reorganization gain (Predecessor XO period). In connection with our audit of the Reorganized XO 2003 consolidated financial statements, we also have audited the 2003 financial statement schedule as listed in the accompanying index. These financial statements and the financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and the financial statement schedule based on our audits. The 2001 consolidated financial statements and financial statement schedule of Predecessor XO, as listed in the accompanying index, were audited by other auditors who have ceased operations. Those auditors' report, dated February 6, 2002, on those financial statements and financial statement schedule was unqualified, before the restatement described in Note 6 to the consolidated financial statements, and included an explanatory paragraph that discussed the substantial doubt about Predecessor XO's ability to continue as a going concern.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 Reorganized XO 2003 consolidated financial statements referred to above present fairly, in all material respects, the financial position of XO Communications, Inc. and subsidiaries as of December 31, 2003, and the results of their operations and their cash flows for the Reorganized XO period in conformity with accounting principles generally accepted in the United States of America. Further, in our opinion, the Predecessor XO 2003 consolidated financial statements referred to above present fairly, in all material respects, the results of their operations and their cash flows for the portion of January 1, 2003 related to the Predecessor's reorganization gain in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the related 2003 financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

As discussed above, the 2001 consolidated financial statements of XO Communications, Inc. as listed in the accompanying index, were audited by other auditors who have ceased operations. As described in Note 5(d), those consolidated financial statements have been restated to conform to Statement of Financial Accounting Standards No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections", which was adopted on January 1, 2003. We audited the adjustments described in Note 5(d) that were applied to restate the 2001 consolidated financial statements. In our opinion, such adjustments are appropriate and have been properly applied. However, we were not engaged to audit, review, or apply any procedures to the 2001 consolidated financial statements of XO Communications, Inc. other than with respect to such adjustments, and, accordingly, we do not express an opinion or any other form of assurance on the 2001 consolidated financial statements taken as a whole.

As discussed in Notes 1, 2, and 3, to the consolidated financial statements, on January 16, 2003, XO Communications, Inc. emerged from bankruptcy. The consolidated financial statements of Reorganized XO reflect the impact of adjustments to reflect the fair value of assets and liabilities under fresh start reporting, which was applied effective January 1, 2003. As a result, the consolidated financial statements of Reorganized XO are presented on a different basis than those of Predecessor XO and, therefore, are not comparable in all respects.

/s/ KPMG LLP

McLean, VA
March 8, 2004

REPORT OF ERNST & YOUNG LLP, INDEPENDENT AUDITORS

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

We have audited the accompanying consolidated balance sheet of XO Communications, Inc. (the "Company") as of December 31, 2002, and the related consolidated statements of operations, stockholders' equity (deficit) and cash flows for the year then ended. Our audit also included the financial statement schedule listed in the Index at item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audit. The consolidated financial statements and schedule of the Company for the year ended December 31, 2001, were audited by other auditors who have ceased operations, and whose report dated February 6, 2002, expressed an unqualified opinion on those consolidated financial statements and schedule before the restatement adjustments described in Note 5 and included an explanatory paragraph that discussed the substantial doubt about the Company's ability to continue as a going concern.

We conducted our audit in accordance with auditing standards generally accepted in the United States. 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 audit provides a reasonable basis for our opinion.

In our opinion, the 2002 financial statements referred to above present fairly, in all material respects, the consolidated financial position of XO Communications, Inc. at December 31, 2002, and the consolidated results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in Note 6 to the consolidated financial statements, effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets".

As discussed in Note 1 to the consolidated financial statements, effective January 16, 2003, the Company was reorganized under a plan of reorganization confirmed by the United States Bankruptcy Court for the Southern District of New York. In connection with its reorganization, the Company will apply fresh start accounting in the first quarter of 2003.

As discussed above, the financial statements of XO Communications, Inc. for the year ended December 31, 2001 were audited by other auditors who have ceased operations. As described in Note 5, these financial statements have been revised to include the transitional disclosures required by Statement of Financial Accounting Standards No. 142, Goodwill and Other Intangible Assets, which was adopted by the Company as of January 1, 2002. Our audit procedures with respect to the disclosures in Note 6 with respect to 2001 included (a) agreeing the previously reported net loss to the previously issued financial statements and the adjustments to reported net loss representing amortization expense recognized in those periods related to goodwill and intangible assets that are no longer being amortized to the Company's underlying records obtained from management, and (b) testing the mathematical accuracy of the reconciliation of adjusted net loss to reported net loss, and the related loss-per-share amounts. In our opinion, the disclosures for 2001 in Note 6 are appropriate. However, we were not engaged to audit, review, or apply any procedures to the 2001 financial statements of the Company other than with respect to such disclosures and, accordingly, we do not express an opinion or any form of assurance on the 2001 financial statements taken as a whole.

/s/ Ernst & Young LLP

Baltimore, Maryland
February 28, 2003

The following report is a copy of a report previously issued by Arthur Andersen LLP ("Andersen"), whose report has not been reissued by Andersen. Certain financial information in the period ended December 31, 2001, was not reviewed by Andersen and includes additional disclosures to conform with new accounting pronouncements and SEC rules and regulations issued during such fiscal year, see Item 1, Business, for discussion of risks.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Stockholders of XO Communications, Inc.:

We have audited the accompanying consolidated balance sheets of XO Communications, Inc. ("XO Parent," a Delaware corporation) and subsidiaries (collectively the "Company") as of December 31, 2001 and 2000, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2001. 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 auditing standards generally accepted in the United States. 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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of XO Communications, Inc. and subsidiaries as of December 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has incurred recurring operating losses and negative cash flows from operating activities, has defaulted on its debt obligations and has begun to implement a proposed recapitalization that contemplates XO Parent filing a voluntary petition for relief under chapter 11 of the United States Bankruptcy Code. These matters, among others, raise substantial doubt about the Company's ability to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. The accompanying consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or the amounts and classification of liabilities that might otherwise be necessary should the Company be unable to continue as a going concern.

Our audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule listed in the index of financial statements is presented for purposes of complying with the Securities and Exchange Commission's rules and is not part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly states, in all material respects, the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

/s/ ARTHUR ANDERSEN LLP

Vienna, VA

February 6, 2002

XO Communications, Inc.

Consolidated Balance Sheets
(Dollars in thousands, except for share and per share data)

	Reorganized XO December 31, 2003	Predecessor XO December 31, 2002
ASSETS		
Current assets:		
Cash and cash equivalents	$ 478,560	$ 314,038
Marketable securities	42,052	246,945
Accounts receivable, net of allowance for doubtful accounts of $32,986 and $37,030 at December 31, 2003 and 2002, respectively	93,958	116,541
Other current assets	12,421	83,480
Total current assets	626,991	761,004
Property and equipment, net	485,984	2,780,589
Broadband wireless licenses and other intangibles, net	109,515	984,614
Other assets, net	42,675	59,289
Total assets	$1,265,165	$ 4,585,496
LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Accounts payable	$ 63,064	$ 63,729
Accrued liabilities	208,353	266,102
Current liabilities subject to compromise	—	5,497,207
Total current liabilities	271,417	5,827,038
Long-term debt and accrued interest payable	536,791	—
Other long-term liabilities	76,532	—
Long-term liabilities not subject to compromise	—	75,242
Long-term liabilities subject to compromise	—	7,182
Total liabilities	884,740	5,909,462
Predecessor XO redeemable preferred stock: par value $0.01 per share, 25,000,000 shares authorized: 7,856,918 shares issued and outstanding, aggregate liquidation preference of $1,693,293, subject to compromise	—	1,708,316
Commitments and contingencies Stockholders' equity (deficit):		
Reorganized XO preferred stock: par value $0.01 per share, 200,000,000 shares authorized: none issued	—	—
Reorganized XO warrants and common stock, par value $0.01 per share, 1,000,000,000 shares authorized: 96,274,140 and 95,000,001 shares issued and outstanding on December 31, 2003 and January 1, 2003, respectively	482,440	—
Reorganized XO subscription rights exercised, 32,503,234 shares authorized: none issued and outstanding	162,516	—
Reorganized XO subscription rights receivable, 32,503,234 shares authorized: none issued and outstanding	(162,516)	—
Predecessor XO common stock, par value $0.02 per share, Class A, 1,000,000,000 shares authorized, 331,033,219 shares issued and outstanding; Class B, 120,000,000 shares authorized, 104,423,158 shares issued and outstanding	—	4,628,139
Deferred compensation	(839)	(8,500)
Accumulated other comprehensive income	1,378	2,512
Accumulated deficit	(102,554)	(7,654,433)
Total stockholders' equity (deficit)	380,425	(3,032,282)
Total liabilities and stockholders' equity (deficit)	$1,265,165	$ 4,585,496

See accompanying notes to the consolidated financial statements.

XO Communications, Inc.

Consolidated Statements of Operations
(Dollars in thousands, except for share and per share data)

	Reorganized XO Year Ended December 31, 2003	Predecessor XO January 1, 2003	Predecessor XO Year Ended December 31, 2002	Predecessor XO Year Ended December 31, 2001
Revenue	$ 1,110,483	$ —	$ 1,259,853	$ 1,258,567
Costs and expenses:				
Cost of service (excludes depreciation and amortization)	422,129	—	522,924	527,698
Selling, operating and general	679,286	—	765,853	1,008,887
Depreciation and amortization	109,308	—	699,806	1,162,671
Restructuring and asset write-downs	11,618	—	480,168	509,202
Total costs and expenses	1,222,341	—	2,468,751	3,208,458
Loss from operations	(111,858)	—	(1,208,898)	(1,949,891)
Investment income (loss), net	46,152	—	16,278	(15,843)
Interest expense, net (contractual interest was $501,118 for the year ended December 31, 2002)	(36,848)	—	(226,451)	(465,401)
Gain on repurchase of debt	—	—	—	345,010
Reorganization gain (expense), net	—	3,032,282	(91,121)	—
Net (loss) income before cumulative effect of accounting change	(102,554)	3,032,282	(1,510,192)	(2,086,125)
Cumulative effect of accounting change	—	—	(1,876,626)	—
Net (loss) income	(102,554)	3,032,282	(3,386,818)	(2,086,125)
Recognition of preferred stock modification fee, net — reorganization item	—	—	78,703	—
Gain on repurchases of preferred stock, net	—	—	—	376,879
Preferred stock dividends and accretion of preferred stock redemption obligation, net (contractual dividend was $98,768 for the year ended December 31, 2002)	—	—	(42,247)	(129,671)
Net (loss) income applicable to common shares	$ (102,554)	$ 3,032,282	$ (3,350,362)	$ (1,838,917)
Net (loss) income per common share, basic and diluted:				
Net (loss) income before cumulative effect of accounting change	$ (1.07)	$ 6.86	$ (3.42)	$ (5.16)
Cumulative effect of accounting change	—	—	(4.24)	—
Net (loss) income	(1.07)	6.86	(7.66)	(5.16)
Recognition of preferred stock modification fee, net — reorganization item	—	—	0.18	—
Gain on repurchases of preferred stock, net	—	—	—	0.93
Preferred stock dividends and accretion of preferred stock redemption obligation, net	—	—	(0.10)	(0.32)
Net (loss) income per common share, basic and diluted	$ (1.07)	$ 6.86	$ (7.58)	$ (4.55)
Weighted average shares, basic and diluted	95,632,859	441,964,342	441,964,342	403,882,956

See accompanying notes to consolidated financial statements.

XO Communications, Inc.

Consolidated Statements of Stockholders' Equity (Deficit)
(Dollars in thousands, except share data)

Predecessor Company	Common Stock Shares Class A	Common Stock Shares Class B	Common Stock Amount	Deferred Compensation	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total
Balance at December 31, 2000	262,010,715	105,414,226	$ 4,392,646	$(72,050)	$(17,041)	$(2,465,154)	$ 1,838,401
Issuance of common and restricted stock in acquisitions	11,211,416	—	29,055	—	—	—	29,055
Issuance of compensatory stock options	—	—	2,551	(2,551)	—	—	
Compensation attributable to stock options and restricted stock vesting	—	—	—	37,173	—	—	37,173
Issuance of common stock through employee benefit plans	11,939,685	—	30,899	—	—	—	30,899
Conversion of Class B common stock into Class A common stock	991,068	(991,068)	—	—	—	—	—
Conversion of 6½% redeemable cumulative preferred stock into Class A common stock	1,621,320	—	17,700	—	—	—	17,700
Issuance of common stock related to equity investment, net of offering costs	50,000,000	—	155,658	—	—	—	155,658
Comprehensive loss:							
Net loss	—	—	—	—	—	(2,086,125)	(2,086,125)
Gain on repurchases of preferred stock, net	—	—	—	—	—	376,879	376,879
Preferred stock dividends and accretion of preferred stock redemption obligation, net	—	—	—	—	—	(129,671)	(129,671)
Other comprehensive income — net unrealized holding gains and foreign currency translation adjustments	—	—	—	—	22,556	—	22,556
Realized net losses transferred to current period earnings	—	—	—	—	4,891	—	4,891
Total comprehensive loss	—	—	—	—	—	—	(1,811,470)
Balance at December 31, 2001	337,774,204	104,423,158	$ 4,628,509	$(37,428)	$ 10,406	$(4,304,071)	$ 297,416
Compensation attributable to stock options and restricted stock vesting	—	—	—	28,928	—	—	28,928
Issuance of common stock through employee benefit plans	85,854	—	24	—	—	—	24
Conversion of 6½% redeemable cumulative preferred stock into Class A common stock	3,173	—	35	—	—	—	35
Conversion of Preferred Stock	23,570	—	—	—	—	—	—
Refund of Employee Stock Purchase Plan funds withheld after cancellation (a)		—	(429)	—	—	—	(429)
Cancellation of Craig McCaw's Class A common stock	(6,853,582)	—	—	—	—	—	—
Comprehensive loss:							
Net loss	—	—	—	—	—	(3,386,818)	(3,386,818)
Recognition of preferred stock modification fee, net - reorganization item	—	—	—	—	—	78,703	78,703
Preferred stock dividends and accretion of preferred stock redemption obligation, net	—	—	—	—	—	(42,247)	(42,247)
Realized net losses and foreign currency translation adjustments transferred to current period earnings	—	—	—	—	(7,894)	—	(7,894)
Total comprehensive loss	—	—	—	—	—	—	(3,358,256)
Balance at December 31, 2002	331,033,219	104,423,158	4,628,139	(8,500)	2,512	(7,654,433)	(3,032,282)
Cancellation of predecessor common sock, deferred compensation, accumulated deficit and accumulated other comprehensive income under Plan of Reorganization	(331,033,219)	(104,423,158)	(4,628,139)	8,500	(2,512)	7,654,433	3,032,282
Balance at January 1, 2003	—	—	$ —	$ —	$ —	$ —	$ —

(a) In the latter half of 2001, the Company's Employee Stock Purchase Plan was cancelled; however employee salary deferrals continued in December 2001, and were subsequently refunded in early 2002.

See accompanying notes to consolidated financial statements.

XO Communications, Inc.

Consolidated Statements of Stockholders' Equity
(Dollars in thousands, except share data)

	Common Stock		Subscription Rights Exercised		Subscription Receivable		Deferred Compensation	Accumulated Deficit	Accumulated Other Comprehensive Income	Total
	Shares	Amount	Shares	Amount	Shares	Amount				
Reorganized Company										
Balance at January 1, 2003	—	$ —	—	$ —	—	$ —	$ —	$ —	$ —	$ —
Issuance of common stock under Plan of Reorganization	95,000,001	475,000	—	—	—	—	—	—	—	475,000
Rights offering	—	—	32,503,234	162,516	(32,503,234)	(162,516)	—	—	—	—
Issuance of common stock through employee benefit plans, net	1,274,139	7,440	—	—	—	—	(839)	—	—	6,601
Comprehensive loss:										
Net loss	—	—	—	—	—	—	—	(102,554)	—	(102,554)
Other comprehensive income - unrealized holding gains arising during the year	—	—	—	—	—	—	—	—	1,378	1,378
Total comprehensive loss	—	—	—	—	—	—	—	—	—	(101,176)
Balance at December 31, 2003	96,274,140	$482,440	32,503,234	$162,516	(32,503,234)	$(162,516)	$(839)	$(102,554)	$1,378	$ 380,425

See accompanying notes to consolidated financial statements.

XO Communications, Inc.

Consolidated Statements of Cash Flows
(Dollars in thousands)

	Reorganized XO Year Ended December 31, 2003	Predecessor XO January 1, 2003	Predecessor XO Year Ended December 31, 2002	Predecessor XO Year Ended December 31, 2001
OPERATING ACTIVITIES:				
Net (loss) income	$(102,554)	$ 3,032,282	$(3,386,818)	$(2,086,125)
Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities:				
Depreciation and amortization	109,308	—	699,806	1,162,671
Accrual of interest	36,791	—	—	—
Stock-based compensation	708	—	28,928	37,173
Non-cash gain on sale of investments	(27,224)	—	—	—
Non-cash restructuring charges and asset write-downs	6,765	—	477,250	598,541
Non-cash reorganization expense, net	—	(3,032,282)	89,448	—
Other income, gain on repurchases of debt, net	—	—	—	(345,010)
Cumulative effect of accounting change	—	—	1,876,626	—
Changes in assets and liabilities, net of effects from acquisitions:				
Accounts receivable	22,583	—	85,514	(43,254)
Other assets	1,317	—	(21,572)	(66,566)
Accounts payable	(7,568)	—	—	—
Accrued liabilities	(33,825)	—	—	—
Other liabilities subject to compromise	—	—	195,904	—
Other liabilities not subject to compromise	—	—	(27,484)	181,693
Net cash provided by (used in) operating activities	6,301	—	17,602	(560,877)
INVESTING ACTIVITIES:				
Capital expenditures, net	(82,346)	—	(208,713)	(1,554,752)
Net releases of pledged securities	—	—	3,161	150
Sales of marketable securities and investments	473,423	—	364,069	2,912,454
Purchases of marketable securities and investments	(238,041)	—	(103,935)	(2,041,247)
Cash received from (paid for) divestitures (acquisitions)	—	—	3,000	(25,203)
Net cash provided by (used in) investing activities	153,036	—	57,582	(708,598)
FINANCING ACTIVITIES:				
Proceeds from borrowings under senior secured credit facility and issuance of notes	—	—	—	1,142,500
Net proceeds from sale of common stock and modification of preferred stock agreement	—	—	—	248,657
Proceeds from issuance of common stock under employee benefit plans	6,452	—	—	30,899
Repurchases of senior notes and redeemable preferred stock	—	—	—	(290,307)
Repayments of capital lease and other obligations	(1,267)	—	(6,079)	(44,124)
Dividends paid on convertible preferred stock	—	—	—	(53,778)
Costs incurred in connection with financing activities	—	—	—	(14,200)
Net cash (used in) provided by financing activities	5,185	—	(6,079)	1,019,647
Effect of exchange rate changes on cash	—	—	(1,256)	3,013
Net increase (decrease) in cash and cash equivalents	164,522	—	67,849	(246,815)
Cash and cash equivalents, beginning of year	314,038	314,038	246,189	493,004
Cash and cash equivalents, end of year	$ 478,560	$ 314,038	$ 314,038	$ 246,189

See accompanying notes to consolidated financial statements.

1. ORGANIZATION AND DESCRIPTION OF BUSINESS

Overview

XO Communications Inc., a Delaware corporation ("XO Parent"), through its subsidiaries, owns and operates an integrated metropolitan and nationwide fiber optic network that provides broadband communication services, local and long distance voice communication services and a wide array of data and integrated data services to business customers in many United States markets. Voice services include local and long distance services, calling card and interactive voice response systems. Data services include Internet access, private data networking and hosting services. XO Parent, through its subsidiaries, also offers integrated combined voice and data services in flat rate "bundled" packages.

Organization

The consolidated financial statements include the accounts and activities of XO Parent, and its subsidiaries (collectively referred to as the "Company" or "XO"). As further discussed in Note 2, on June 17, 2002 (the "Petition Date"), XO Parent filed a voluntary petition for relief under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") with the United States Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court"). On January 16, 2003 (the "Effective Date"), XO Parent emerged from the Bankruptcy Court proceedings pursuant to the terms of its third amended plan of reorganization (the "Plan of Reorganization"). Accordingly, the accompanying consolidated financial statements have been prepared in accordance with Statement of Position 90-7, "Financial Reporting by Entities in Reorganization under the Bankruptcy Code," ("SOP 90-7"). As discussed in Note 3, the Company implemented fresh start accounting under the provisions of SOP 90-7. Under the fresh start accounting provisions of SOP 90-7, the fair value of the reorganized Company was allocated to its assets and liabilities, and its accumulated deficit was eliminated. Predecessor financial statements are not comparable to the financial statements of the Reorganized Company.

On February 19, 2004, the United States Bankruptcy Court for the Southern District of New York approved the Asset Purchase Agreement by and between XO Parent and Allegiance Telecom, Inc., or Allegiance, pursuant to which XO Parent has agreed to acquire substantially all of the assets of Allegiance for approximately $311.0 million in cash and approximately 45.4 million shares of XO's common stock. XO anticipates that the acquisition of the Allegiance assets will close during the third quarter of 2004. See Note 22 for additional disclosure.

2. REORGANIZATION

On the Effective Date, XO Parent consummated its Plan of Reorganization and emerged from its Chapter 11 reorganization proceedings with a significantly restructured balance sheet. The consummation of the Plan of Reorganization resulted in the following changes in XO Parent's capital structure:

- The conversion of $1.0 billion of loans under its pre-petition secured credit facility into $500.0 million of outstanding principal amount under an amended and restated credit agreement (the "Credit Facility");
- The extinguishment of all amounts due under its pre-petition unsecured senior and subordinated notes and certain general unsecured obligations;
- The cancellation of all outstanding shares and interests in its pre-petition preferred stock and pre-petition common stock; and

- The issuance of approximately 95.0 million shares of common stock of the reorganized Company ("New Common Stock") and warrants to purchase up to an additional 23.75 million shares of New Common Stock of the reorganized Company.

The following table shows the distribution each party of interest impacted by XO Parent's bankruptcy was entitled to. As certain claims are still being reviewed by the Bankruptcy Court, proportional distributions have not yet been made and cannot be made until the court rules (dollars in thousands except share data).

Party of Interest	Shares of New Common Stock	Series A Warrants	Series B Warrants	Series C Warrants	Credit Facility	Cash
$1 Billion senior secured credit facility	90,250,001	—	—	—	$500,000	$ —
Senior unsecured notes	4,715,344	9,430,689	7,073,015	7,073,015	—	1,600
Subordinated notes	—	—	—	—	—	616
General unsecured creditors	34,656	69,309	51,980	51,980	—	403
Total entitlement	95,000,001	9,499,998	7,124,995	7,124,995	$500,000	$2,619
Not yet distributed	1,230,638	2,461,743	1,846,151	1,846,151	—	1,612
Total issued or paid	93,769,363	7,038,255	5,278,844	5,278,844	$500,000	$1,007

See notes 13 and 14 for further disclosure on our equity and debt instruments

In accordance with the Plan of Reorganization, XO Parent issued to certain holders of claims of interest in XO Parent, who held such claims and/or interests as of the November 15, 2002 record date, rights to subscribe for up to 40.0 million shares of New Common Stock, at $5.00 per share, through a rights offering, (the "Rights Offering"). The first stage of the Rights Offering closed on November 14, 2003 whereby $162.5 million in cash for 32.5 million shares was placed into escrow until the conclusion of the second stage. On January 5, 2004, XO Parent concluded the second stage of its Rights Offering. An aggregate of 39.7 million shares were issued in the offering, yielding net proceeds of $197.6 million. These proceeds were used to pay down the Credit Facility. The following unaudited pro forma information shows the impact to XO's historical balance sheet as of December 31, 2003 as a result of these transactions (dollars in thousands):

	December 31, 2003	Rights Offering Adjustments	Pro forma December 31, 2003
		(Unaudited)	(Unaudited)
Long-term debt	$ 536,791	$(197,612)	$ 339,179
Total liabilities	884,740	(197,612)	687,128
Total stockholders' equity (deficit)	380,425	197,612	578,037
Total liabilities and stockholders' equity (deficit)	$1,265,165	$ —	$1,265,165

3. FRESH START ACCOUNTING

The Company adopted the fresh start accounting provisions ("fresh start") of SOP 90-7 during the first quarter of 2003. Under SOP 90-7, the implementation of fresh start reporting is triggered in part by the emergence of XO Parent from its Chapter 11 proceedings. Although the Effective Date of the Plan of Reorganization was January 16, 2003, due to the immateriality of the results of operations for the period between January 1, 2003 and the Effective Date, the Company accounted for the consummation of the Plan of Reorganization as if it had occurred on January 1, 2003 and implemented fresh start reporting as of that date. Fresh start requires that the Company adjust the historical cost of its assets and liabilities to their fair value. The fair value of the reorganized Company, or the reorganization value, of approximately $1.3 billion was determined based on the negotiated sum of the reorganized Company's liabilities and equity that were issued and outstanding after final negotiations and Bankruptcy Court approval. These included $500.0 million of debt outstanding under the Credit Agreement, $475.0 million of New Common Stock, and $373.1 million of other liabilities that were not eliminated or discharged under the Plan of Reorganization.

Fresh start requires that the reorganization value be allocated to the entity's net assets in conformity with procedures specified by SFAS No. 141, "Business Combinations," ("SFAS No. 141"). The Company engaged an independent appraiser to assist in the allocation of the reorganization value to the reorganized Company's assets and liabilities by determining the fair market value of its property and equipment, intangible assets and certain obligations related to its facility leases. A reconciliation of the adjustments to be recorded in connection with effecting the Plan of Reorganization and adopting fresh start accounting is presented below (dollars in thousands):

	Predecessor XO December 31, 2002	Reorganization	Fresh Start Adjustments(d)	Reorganized XO January 1, 2003
ASSETS				
Current assets:				
Cash and cash equivalents	$ 314,038	$ —	$ —	$ 314,038
Marketable securities	246,945	—	—	246,945
Accounts receivable, net	116,541	—	—	116,541
Other current assets	83,480	—	(48,288)	35,192
Total current assets	761,004	—	(48,288)	712,716
Property and equipment, net	2,780,589	—	(2,304,001)	476,588
Broadband wireless licenses and other intangibles, net	984,614	—	(848,936)	135,678
Other assets, net	59,289	—	(36,181)	23,108
Total assets	$ 4,585,496	$ —	$(3,237,406)	$1,348,090
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY				
Current liabilities:				
Accounts payable	$ 63,729	$ —	$ 3,539	$ 67,268
Accrued liabilities	266,102	—	(30,910)	235,192
Current liabilities subject to compromise	5,497,207	(5,466,667) (a)	(30,540)	—
Total current liabilities	5,827,038	(5,466,667)	(57,911)	302,460
Long-term debt —	—	500,000 (b)	—	500,000
Other long-term liabilities	75,242	—	(4,612)	70,630
Long-term liabilities subject to compromise	7,182	—	(7,182)	—
Total liabilities	5,909,462	(4,966,667)	(69,705)	873,090
Predecessor XO redeemable preferred stock — subject to compromise	1,708,316	(1,708,316) (a)	—	—
Stockholders' (deficit) equity:				
Predecessor XO common stock	4,628,139	—	(4,628,139)	—
Reorganized XO common stock and warrants	—	475,000 (c)	—	475,000
Deferred compensation	(8,500)	—	8,500	—
Accumulated other comprehensive income	2,512	—	(2,512)	—
Accumulated deficit	(7,654,433)	6,199,983 (e)	1,454,450	—
Total stockholders' (deficit) equity	(3,032,282)	6,674,983	(3,167,701) (e)	475,000
Total liabilities and stockholders' (deficit) equity	$ 4,585,496	$ —	$(3,237,406)	$1,348,090

(a) To record the discharge of pre-petition indebtedness, including a $1.0 billion credit facility, $4.2 billion of senior and convertible subordinated notes, $245.2 million of accrued interest, and the elimination of $1.7 billion of pre-petition redeemable preferred stock and $50.6 million of accrued dividends, all in accordance with the Plan of Reorganization.

(b) To record the outstanding principal under the Credit Agreement, in accordance with the Plan of Reorganization.

(c) To record the issuance of 95.0 million shares of New Common Stock and warrants in accordance with the Plan of Reorganization. Participation in the Rights Offering was recorded in the first quarter of 2004.

(d) To adjust the carrying value of assets, liabilities and stockholders' equity to fair value, in accordance with fresh start.

(e) Net reorganization gain on January 1, 2003 consisted of the following (dollars in thousands):

Net gain resulting from reorganization of debt, preferred stock and equity	$ 6,199,983
Net loss resulting from fresh start fair value adjustments to assets and liabilities	(3,167,701)
Total reorganization gain, net	$ 3,032,282

4. ACCOUNTING IMPACT OF CHAPTER 11 FILING

Liabilities subject to compromise reflected in the accompanying consolidated financial statements for Predecessor XO and the XO Parent stand-alone financial statements represent the liabilities of XO Parent incurred prior to the Petition Date. In accordance with SOP 90-7, liabilities subject to compromise were recorded at the amount allowed on pre-petition claims in the Chapter 11 proceedings. Other obligations that were not subject to compromise retained their historical balance sheet classifications and amounts. Liabilities subject to compromise consisted of the following as of December 31, 2002 (dollars in thousands):

Long-term debt	$5,165,718
Accrued interest and preferred stock dividends	295,820
Pre-petition accounts payable and accrued liabilities	33,640
Capital lease obligations	9,211
Total liabilities subject to compromise	5,504,389
Less: long-term liabilities subject to compromise	7,182
Current liabilities subject to compromise	$5,497,207

In order to record its debt instruments at the amount allowed by the Bankruptcy Court in accordance with SOP 90-7, as of the Petition Date, XO Parent wrote off all of its debt issuance costs and discounts related to debt (collectively the "Deferred Financing Fees") as a component of reorganization expense. Reorganization expense also included professional fees incurred in connection with the Chapter 11 proceedings, as well as gains or penalties from the settlement or rejection of liabilities subject to compromise and the net gains from the investment termination payment received as a settlement during the bankruptcy process. Reorganization expenses for the year ended December 31, 2002 consisted of the following (dollars in thousands):

Net loss from the settlement or rejection of liabilities subject to compromise	$ 14,916
Net gain from investment termination payment	(16,667)
Deferred Financing Fees	56,270
Professional fees	36,602
Total reorganization expense, net	$ 91,121

Under SOP 90-7, XO Parent was required to accrue interest expense during the Chapter 11 proceedings only to the extent that such interest was expected to be paid pursuant to the proceedings. Under the Plan of Reorganization, there were no cash payments of interest on the loans outstanding under the $1.0 billion pre-petition credit facility or XO Parent's unsecured notes. Therefore, XO Parent ceased accruing interest on the pre-petition credit facility and on its unsecured notes from the Petition Date through the Effective Date.

In accordance with SOP 90-7, XO Parent recorded its preferred stock at the amount allowed by the Bankruptcy Court. Accordingly, as of the Petition Date, XO Parent recognized a gain equal to the remaining $81.5 million unamortized balance of a deferred modification fee and wrote off all issuance costs and discounts related to its preferred stock, which resulted in a charge of $2.8 million. In addition, the Company stopped accruing preferred stock dividends subsequent to the Petition Date.

XO Parent Stand-Alone Financial Statements

In accordance with SOP 90-7, stand-alone financial statements of XO Parent are presented below. Such financial statements have been prepared using standards consistent with the Company's consolidated financial statements without eliminating intercompany transactions and without consolidating controlled subsidiaries (dollars in thousands).

XO Communications, Inc.
(XO Parent)
Debtor in Possession
Stand-Alone Balance Sheet
As of December 31, 2002
(Unaudited)

ASSETS	
Current assets:	
Pledged securities	$ 1,100
Other current assets	66,764
Total current assets	67,864
Property and equipment, net	65,654
Broadband wireless licenses, net	67,039
Other intangibles, net	79,711
Investment in and notes receivable from subsidiaries, net	8,542,749
Other assets, net	43,638
Total assets	$ 8,866,655
LIABILITIES AND STOCKHOLDERS' EQUITY	
Current liabilities not subject to compromise	$ 50,422
Debt and accrued interest payable to subsidiary subject to compromise	620,389
Current liabilities subject to compromise	5,497,207
Total current liabilities	6,168,018
Long-term liabilities not subject to compromise	62,633
Long-term liabilities subject to compromise	7,182
Total liabilities	6,237,833
Redeemable preferred stock held by and payable to a subsidiary subject to compromise	514,640
Redeemable preferred stock subject to compromise	1,708,316
Stockholders' equity:	
Common stock	4,628,139
Deferred compensation	(8,149)
Accumulated deficit	(4,214,124)
Total stockholders' equity	405,866
Total liabilities and stockholders' equity	$ 8,866,655

XO Communications, Inc.
(XO Parent)
Debtor in Possession
Stand-Alone Statement of Operations
(Unaudited)

	Period from the Petition Date of June 17, 2002 through December 31, 2002
Revenue	$ —
Costs and expenses:	
Selling, operating, and general (excludes stock based compensation)	75,000
Stock-based compensation	12,352
Depreciation and amortization	47,584
Total costs and expenses	134,936
Loss from operations	(134,936)
Reorganization expense, net	(91,121)
Interest income on notes receivable from subsidiaries	286,202
Interest expense	(3,468)
Net income	56,677
Recognition of preferred stock modification fee, net - reorganization item	78,703
Net income applicable to common shares	$ 135,380

XO Communications, Inc.
(XO Parent)
Debtor in Possession
Stand-Alone Statement of Cash Flows
(Unaudited)

	Period From the Petition Date of June 17, 2002 through December 31, 2002
OPERATING ACTIVITIES:	
Net income	$ 56,677
Adjustments for non-cash items:	
Depreciation and amortization	47,584
Reorganization expense	91,121
Stock-based compensation	12,352
Interest income on notes receivable from subsidiaries	(286,202)
Interest expense	3,468
Changes in assets and liabilities:	
Notes receivable from subsidiaries, net	75,000
Net cash used in operating activities	—
Net increase (decrease) in cash and cash equivalents	—
Cash and cash equivalents, beginning of the period	—
Cash and cash equivalents, end of period	$ —

5. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Review of Significant Accounting Policies

As discussed in Note 3, the Company adopted fresh start as of January 1, 2003, creating, in substance, per SOP 90-7, a new reporting entity. The reorganized Company has adopted the policy of expensing customer installation costs and internal labor directly associated with network construction in the period in which the costs are incurred as this labor effort is not specific to any large segregated project, but rather to ordinary course business operations. The predecessor Company capitalized and amortized these costs. In accordance with SOP 90-7, the reorganized Company was also required to implement newly issued accounting pronouncements that would require adoption within twelve months of applying fresh start.

(b) Principles of Consolidation

The Company's consolidated financial statements include all of the assets, liabilities and results of operations of subsidiaries in which the Company has a controlling interest. All inter-company accounts and transactions among consolidated entities have been eliminated.

(c) Preparation of Consolidated Financial Statements

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Management periodically assesses the accuracy of these estimates and assumptions. Actual results could differ from those estimates.

Certain reclassifications have been made to prior period amounts in order to conform to the current year presentation. Such reclassifications had no effect on net loss or total stockholders' equity.

(d) Adoption of SFAS No. 145

Effective January 1, 2003, the Company adopted SFAS No. 145, "Rescission of the Financial Accounting Standards Board Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections as of April 2002" ("SFAS No. 145"), which eliminates the requirement to report material gains or losses from debt extinguishments as an extraordinary item, net of any applicable income tax effect, in an entity's statement of operations. SFAS No. 145 instead requires that a gain or loss recognized from a debt extinguishment be classified as an extraordinary item only when the extinguishment meets the criteria of both "unusual in nature" and "infrequent in occurrence" as prescribed under APB Opinion No. 30, "Reporting the Results of Operations — Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" ("APB No. 30"). Upon adopting SFAS No. 145, the Company reclassified a 2001 $345.0 million gain from debt repurchases from extraordinary to recurring.

(e) 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. Cash equivalents consist primarily of money market accounts that are available on demand. The carrying amount of these instruments approximates fair value due to their short maturities.

(f) Marketable Securities

Substantially all of the Company's marketable securities currently consist of investments in publicly traded companies. The Company classifies investments in equity securities as available-for-sale and records such investments at fair value. The fair values are based on quoted market prices. Investments in debt securities are recorded at cost, which approximates fair value, as the debt trades in a thin market. Unrealized gains and losses on available-for-sale marketable securities are reported as a separate component of comprehensive income. Realized gains and losses for available-for-sale securities are recognized in investment income.

(g) Long-Lived Assets

Long-lived assets include property and equipment, broadband wireless licenses, and intangible assets to be held and used. Long-lived assets, excluding intangible assets with indefinite useful lives, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount should be addressed pursuant to SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," ("SFAS No. 144"). The criteria for determining impairment for such long-lived assets to be held and used is determined by comparing the carrying value of these long-lived assets to management's best estimate of future undiscounted cash flows expected to result from the use of the assets. The Company believes that no impairment existed under SFAS No. 144 as of December 31, 2003. In the event that there are changes in the planned use of the Company's long-lived assets or its expected future undiscounted cash flows are reduced significantly, the Company's assessment of its ability to recover the carrying value of these assets under SFAS No. 144 could change.

Intangible assets with indefinite useful lives are tested for impairment annually during the fourth quarter, or more frequently if an event indicates that the asset might be impaired in accordance with SFAS No. 142, "Goodwill and Other Intangible Assets." The Company believes that there was no impairment of its intangible assets with indefinite useful lives as of December 31, 2003.

(h) Property and Equipment

Property and equipment acquired prior to December 31, 2002 is stated at its fair value at January 1, 2003, as required by fresh start. Additions to property and equipment during 2003 are stated at cost. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets beginning in the month telecommunications networks and acquired bandwidth are substantially complete and available for use and in the month equipment and furniture are acquired. Telecommunications networks and bandwidth include the deployment of fiber optic cable and telecommunications hardware and software for the expressed purpose of delivering telecommunications services. Costs of additions and improvements are capitalized, and repairs and maintenance are charged to expense as incurred. Direct external costs of constructing property and equipment are capitalized including interest costs related to construction. The reorganized Company has adopted the policy of expensing internal labor directly associated with network construction in the period in which the costs are incurred as this labor effort is not specific to any large segregated project.

Equipment held under capital leases is stated at the lower of the fair value of the asset or the net present value of the minimum lease payments at the inception of the lease. For equipment held under capital leases, depreciation is provided using the straight-line method over the shorter of the estimated useful lives of the leased assets or the related lease term.

The estimated useful lives of property and equipment are as follows:

Telecommunications networks and acquired bandwidth	3-20 years
Furniture, fixtures, equipment, and other	5-7 years
Leasehold improvements	the shorter of the estimated or the terms of the leases useful lives

These useful lives are determined based on historical usage with consideration given to technological changes and trends in the industry, which could impact the network architecture and asset utilization. Accordingly, in making this assessment, the Company considers its planned use of the assets, the views of experts within the Company and outside sources regarding the impact of technological advances and trends in the industry on the value and useful lives of its network assets. The Company periodically evaluates the estimated useful lives used to depreciate its assets. While the Company believes its estimate of useful lives are reasonable, significant differences in actual experience or significant changes in assumptions may affect future depreciation expenses.

(i) Broadband Wireless Licenses and Other Intangibles

Broadband wireless licenses were stated at their fair values at January 1, 2003, as required by fresh start. The reorganized Company is amortizing these licenses over an estimated useful life of 10 years based on the initial license term granted by the Federal Communications Commission. Amortization commences when commercial service using broadband wireless technology is deployed in the license's geographic area.

Other intangibles of the Company are valued at fair value as required by the provisions of fresh start and SFAS No. 141 and consist of customer relationships, internally developed technology and XO's trade name. The customer relationships and internally developed technology are being amortized using the straight-line method over their estimated useful lives of three years. The XO trade name was determined to have an indefinite life. Accordingly, it is not subject to amortization.

(j) Goodwill

Goodwill consisted primarily of goodwill from the Concentric merger. Effective January 1, 2002, the Company adopted SFAS No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"). The Company performed the required transitional impairment tests of goodwill as of January 1, 2002, and determined that the goodwill was totally impaired. Accordingly, in the first quarter of 2002 the Company recognized a $1,876.6 million charge as a cumulative effect of accounting change to write off all of its goodwill.

(k) Other Assets

Other assets consist primarily of escrow and security deposits and pledged securities. The escrow and security deposits and pledged securities are stated at cost, and their fair value approximates their carrying value.

(l) Income Taxes

The Company accounts for income taxes in accordance with the provisions of SFAS No. 109, "Accounting for Income Taxes," ("SFAS No. 109") which requires that deferred income taxes are 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. Valuation allowances are used to reduce deferred tax assets to the amount considered likely to be realized. The provisions of SFAS No. 109 have been applied as if the Company were a separate tax payer.

(m) Revenue Recognition

Revenues from telecommunications services are recognized when the services are performed, evidence of an arrangement exists, the fee is fixed and determinable and collectibility is probable. In circumstances when these criteria are not met, revenue recognition is deferred until resolution occurs.

Service discounts and incentives related to telecommunication services are recorded as a reduction of revenue when granted or ratably over a contract period. Fees billed in connection with service installations and other non-recurring charges are deferred and recognized ratably over the estimated customer life.

The Company establishes allowances for collection of doubtful accounts and other sales credit adjustments. Allowances for sales credits are established through a charge to revenue, while allowances for doubtful accounts are established through a charge to selling, operating and general expense. The Company assesses the adequacy of these reserves monthly by considering general factors, such as the length of time individual receivables are past due, historical collection experience, the economic and competitive environment, and changes in the creditworthiness of its customers. The Company believes that the established valuation allowances were adequate as of December 31, 2003. If circumstances relating to specific customers change or economic conditions worsen such that the Company's past collection experience and assessment of the economic environment are no longer relevant, XO's estimate of the recoverability of its trade receivables could be further reduced.

Revenue from the sale or lease of unlit network capacity is recognized upon consummation of the transaction and the acquirer's acceptance of the capacity in instances when the Company receives upfront cash payments and is contractually obligated to transfer title to the specified capacity at the end of the contract term. If the transaction does not meet these criteria, revenue is recognized ratably over the contract term. There were no sales of unlit capacity during the reported periods whereby revenue was recognized "up front" upon consummation of the transaction.

(n) Cost of Service

Cost of service includes expenses directly associated with providing telecommunications services to customers, including, among other items, the cost of connecting customers to the Company's networks via leased facilities, the costs of leasing components of our network facilities and costs paid to third party providers for interconnect access and transport services. All such costs are expensed as incurred. The Company accrues for the expected costs of services received from third party telecommunications providers during the period the services are rendered. Invoices received from the third party telecommunications providers are often disputed due to billing discrepancies. The Company accrues for all invoiced amounts, even amounts in dispute, as these amounts represent contingent liabilities that are considered probable and measurable. Disputes resolved in the Company's favor may reduce cost of service in the period the dispute is settled and typically reflect costs paid in the prior periods. Because the period of time required to resolve these types of disputes often lapses over several quarters, the benefits associated with the favorable resolution of such disputes normally are realized in periods subsequent to the accrual of the disputed invoice.

(o) Net Income (Loss) Per Share

Net income (loss) per common share, basic and diluted, is computed by dividing net income (loss) applicable to common shares by the weighted average number of common shares outstanding for the period. In periods of net loss, the assumed common share equivalents for options and warrants are anti-dilutive.

(p) Stock-Based Compensation

Effective January 1, 2003, the Company adopted the disclosure provisions of SFAS No. 148, "Accounting for Stock-Based Compensation — Transition and Disclosure," ("SFAS No. 148"). This statement amends SFAS No. 123, "Accounting for Stock-Based Compensation," ("SFAS No. 123"), to provide for alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, this statement amends the disclosure provisions of SFAS No. 123 and APB No. 28, "Interim Financial Reporting," ("APB No. 28") to require disclosure in the summary of significant accounting policies of the effects of an entity's accounting policy with respect to stock-based employee compensation on reported net income and earnings per share in annual and interim financial statements.

As allowed by SFAS No. 148, the Company has chosen to continue to account for compensation cost associated with its employee stock plan in accordance with the intrinsic value method prescribed by APB No. 25, "Accounting for Stock Issued to Employees," ("APB No. 25") adopting the disclosure-only provisions of SFAS No. 123. Under this method, no compensation expense is recorded if stock options are granted at an exercise price equal to or greater than the fair market value of the Company's stock on the grant date. If the Company had adopted the fair value method of accounting for its stock awards, stock-based compensation would have been determined based on the fair value for all stock awards at the grant date using a Black-Scholes pricing model and the following weighted average assumptions:

	Reorganized XO 2003	Predecessor XO 2002	Predecessor XO 2001
Expected volatility	75.0%	125.0%	125.0%
Risk free interest rate	2.6%	4.0%	4.3%
Dividend yield	0.0%	0.0%	0.0%
Expected life (range in years)	4.0	4.0	4.0
Fair value per share at grant date	$2.95	$ 0.11	$ 5.10

The Company's pro forma net loss applicable to common shares, and pro forma net loss per common share, basic and diluted, if the Company had used the fair value method would have been as follows (dollars in thousands, except per share data):

	Reorganized XO December 31, 2003	Predecessor XO December 31, 2002	Predecessor XO December 31, 2001
Net loss applicable to common shares, as reported	$(102,554)	$(3,350,362)	$(1,838,917)
Add: Stock-based employee compensation expense included in net loss applicable to common shares, as reported	708	28,928	37,173
Deduct: Total stock-based employee compensation expense determined under fair value based methods for all stock awards, net of related tax effects	(16,189)	(1,462)	(44,138)
Pro forma net loss	$(118,035)	$(3,322,896)	$(1,845,882)
Net loss per common share, basic and diluted:			
Net loss per common share, basic and diluted - as reported	$ (1.07)	$ (7.58)	$ (4.55)
Net loss per common share, basic and diluted - pro forma	$ (1.23)	$ (7.52)	$ (4.57)

(q) Comprehensive Loss

Comprehensive loss includes the Company's net loss applicable to common shares, as well as net unrealized gains and losses on available-for-sale investments and, for any periods prior to the second quarter of 2002, foreign currency translation adjustments relating to the Company's European operations, which were disposed of in February 2002.

(r) Concentration of Credit Risk

Other financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of trade receivables. Although the Company's trade receivables are geographically dispersed and include customers in many different industries, a portion of the Company's revenue is generated from services provided to other telecommunications service providers. Several of these companies have filed for protection under Chapter 11 of the Bankruptcy Code while others have experienced business downturns. The Company believes that its established valuation and credit allowances are adequate to cover these risks.

(s) Fair Value of Financial Instruments

SFAS No. 107, "Disclosure about Fair Value of Financial Instruments" ("SFAS No. 107"), requires disclosure of fair value information about financial instruments, for which it is practicable to estimate the value. The carrying amounts for the majority of the Company's financial instruments classified as current assets and liabilities approximate their fair value due to their short maturities. Marketable securities are recorded at fair value. Amounts outstanding under long-term debt agreements approximate their estimated fair values as they accrue interest at rates that are variable every 3-6 months.

(t) Recent Accounting Pronouncements

In June 2001, the Financial Accounting Standards Board, ("FASB") issued SFAS No. 143, "Accounting for Asset Retirement Obligations," ("SFAS No. 143"), which requires an entity to recognize the fair value of a liability for an asset retirement obligation in the period in which a legal or contractual removal obligation is incurred if a reasonable estimate of fair value can be made. If a reasonable estimate of fair value cannot be made in the period the asset retirement obligation is incurred, SFAS No. 143 requires the liability to be recognized when a reasonable estimate of the fair value can be made. As required by SOP 90-7, we implemented SFAS No. 143 on January 1, 2003, in conjunction with the implementation of fresh start and recorded an estimated asset retirement obligation of $12.0 million, as disclosed in Note 12.

Effective January 1, 2003, the Company adopted SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities" ("SFAS No. 146"), which requires that costs, including severance costs, associated with exit or disposal activities be recorded at their fair value when a liability has been incurred. Under previous guidance, certain exit costs, including severance costs, were accrued upon managements' commitment to an exit plan, which is generally before an actual liability has been incurred. The adoption of SFAS No. 146 did not have a material effect on the Company's consolidated financial statements.

In May 2003, the FASB issued SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities," ("SFAS No. 149"), which amends and clarifies accounting for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities under SFAS No. 133. SFAS No. 149 is effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. The adoption of SFAS No. 149 did not have a material impact on the Company's consolidated financial statements.

In May 2003, the FASB issued SFAS No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity," ("SFAS No. 150"), which establishes standards for how companies classify and measure certain financial instruments with characteristics of both liabilities and equity. It requires companies to classify a financial instrument that is within its scope as a liability (or an asset in some circumstances). SFAS No. 150 is effective beginning with the second quarter of fiscal 2003. The adoption of SFAS No. 150 did not have a material impact on the Company's consolidated financial statements.

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities," an interpretation of Accounting Research Bulletin No. 51, "Consolidated Financial Statements" ("FIN 46"). FIN 46 applies to any business enterprise that has a controlling interest, contractual relationship or other business relationship with a variable interest entity ("VIE") and establishes guidance for the consolidation of VIEs that function to support the activities of the primary beneficiary. In December 2003, the FASB completed its deliberations regarding the proposed modification to FIN 46 and issued Interpretation Number 46R, "Consolidation of Variable Interest Entities-an Interpretation of ARB No. 51" ("FIN 46R"). The decision reached included a deferral of the effective date and provisions for additional scope exception for certain type of variable interests. Application of FIN 46R is required in financial statements of public entities that have interests in VIEs or potential VIEs commonly referred to as special-purpose entities for period ending after December 15, 2003. Application by public entities (other than small business issuers) for all other types of entities is required in financial statements for periods ending after March 15, 2004. The Company does not believe that the adoption of FIN 46R will have any effect on the Company's consolidated financial statements.

In November 2002, the FASB's Emerging Issues Task Force reached a final consensus on Issue No. 00-21. "Accounting for Revenue arrangements with Multiple Deliverables" ("EITF 00-21"), which is effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. Under the EITF 00-21, revenue arrangements with multiple deliverables are required to be divided into separate units of accounting under certain circumstances. The adoption of EITF 00-21 did not have a material effect on the Company's consolidated financial statements.

In December 2003, the SEC issued Staff Accounting Bulletin No. 104, "Revenue Recognition", which updates the guidance in SAB No. 101, integrates the related set of Frequently Asked Questions, and recognizes the role of EITF 00-21. The adoption of SAB No. 104 did not have a material effect on the Company's consolidated financial statements.

6. CUMULATIVE EFFECT OF ACCOUNTING CHANGE

Effective January 1, 2002, the Company adopted SFAS No. 142 and performed the required transitional impairment tests of goodwill, and determined that the value of its goodwill was totally impaired. Accordingly, in the first quarter of 2002, the Company recorded a $1,876.6 million charge as a cumulative effect of accounting change to write-off all of its goodwill. The adjusted net loss and related earnings per share before cumulative effect of accounting change for the year ended December 31, 2001 compared to the actual results for the years ended December 31, 2003 and 2002 is as follows (dollars in thousands, except per share data):

	Reorganized XO	Predecessor XO	
	2003	2002	2001
Reported net loss before cumulative effect of accounting change	$(102,554)	$(1,510,192)	$(2,086,125)
Goodwill amortization	—	—	595,601
Adjusted net loss before cumulative effect of accounting change	$(102,554)	(1,510,192)	(1,490,524)
Net loss per common share before cumulative effect of accounting change, basic and diluted:			
Reported net loss before cumulative effect of accounting change	$ (1.07)	$ (3.42)	$ (5.16)
Goodwill amortization	—	—	1.47
Adjusted net loss per common share before cumulative effect of accounting change, basic and diluted	$ (1.07)	$ (3.42)	$ (3.69)

7. RESTRUCTURING CHARGES AND ASSET WRITE-DOWNS

During 2003, the Company recorded restructuring charges of $11.6 million from the reduction of its work force by approximately 550 employees, primarily employed in network operations, sales and marketing and information technology and estimated losses associated with restructured leases. During the second half of 2001, and the first half of 2002, the Company implemented a plan to restructure certain of its business operations. The restructuring plan included divesting its European operations and reducing the Company's discretionary spending, capital expenditures and workforce based on its assessment at that time of current and expected future market conditions.

As of December 31, 2003, the remaining restructuring accrual was $60.0 million, which relates primarily to payments due to landlords on exited leased facilities. The restructuring accrual has decreased from $79.0 million as of December 31, 2002, due to $17.2 million in payments associated with exited leased facilities and $40.3 million of non-cash reductions made in conjunction with the Company's implementation of fresh start to reflect the December 31, 2002 accrual at its estimated net present value offset by a $26.8 million increase from reorganization adjustments.

8. MARKETABLE SECURITIES

Marketable securities consisted of the following (dollars in thousands):

	Reorganized XO December 31, 2003	Predecessor XO December 31, 2002
Investments in equity and debt securities	$42,052	$ —
U.S. Government and agency notes and bonds	—	246,945
	$42,052	$246,945

The amortized cost, gross unrealized gains and losses and fair value of the investment securities available-for-sale as of December 31, 2003 and 2002, are as follows (dollars in thousands):

	Fair Value	Cost Basis	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses
As of December 31, 2003				
Equity securities	$ 30,041	$ 28,663	$3,001	$(1,623)
Debt securities	12,011	12,011	—	—
Total marketable securities	$ 42,052	$ 40,674	$3,001	$(1,623)
As of December 31, 2002				
U.S. Governments and agency notes and bonds	$246,945	$244,433	$2,512	$ —

Debt securities as of December 31, 2003 mature in 2007.

9. PROPERTY AND EQUIPMENT

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

	Reorganized XO December 31, 2003	Predecessor XO December 31, 2002
Telecommunications networks and acquired bandwidth	$407,747	$2,920,819
Furniture, fixtures, equipment, and other	77,783	656,994
	485,530	3,577,813
Less accumulated depreciation	79,501	1,165,216
	406,029	2,412,597
Network construction-in-progress	79,955	367,992
	$485,984	$2,780,589

As discussed in Note 3, the Company applied fresh start on January 1, 2003. Accordingly its property and equipment as of January 1, 2003, were recorded at fair value which resulted in a significant write down of property and equipment and a reduction in the associated depreciation expense in 2003. During 2003, 2002 and 2001, depreciation expense was $83.1 million, $598.5 million and $447.0 million, respectively. During 2003, 2002 and 2001 the Company capitalized interest on construction costs of $3.0 million, $11.1 million, and $51.6 million, respectively. Assets classified as construction-in-progress are not being depreciated as they are not currently ready for their intended use.

10. BROADBAND WIRELESS LICENSES AND OTHER INTANGIBLES

Broadband wireless licenses and other intangible assets consisted of the following (dollars in thousands):

	Reorganized XO December 31, 2003	Predecessor XO December 31, 2002
Broadband wireless licenses	$ 59,508	$ 997,942
Customer relationships	49,987	123,745
Internally developed technology	9,521	—
Acquired technology	—	130,515
Other	—	35,413
	119,016	1,287,615
Less accumulated amortization	(26,163)	(303,001)
	92,853	984,614
XO Trade name — indefinite life asset	16,662	—
	$109,515	$ 984,614

As discussed in Note 3, the Company applied fresh start on January 1, 2003. Accordingly its broadband wireless licenses and other intangibles as of January 1, 2003, were recorded at fair value which resulted in a significant write down of broadband wireless licenses and other intangibles and a reduction in the associated amortization expense in 2003. Amortization expense for the years ended December 31, 2003, 2002 and 2001 was $26.2 million, $101.3 million and $715.7 million, respectively. Broadband wireless licenses are amortized when commercial service using the wireless technology is deployed in the license's geographic area. As of December 31, 2003, approximately $23.5 million of broadband wireless licenses are not being amortized as commercial services have not been deployed in the license's geographic area. Estimated amortization expense for the next five years is $26.1 million, $26.1 million, $6.3 million, $6.3 million and $4.4 million, respectively.

11. ACCRUED LIABILITIES

Accrued liabilities consisted of the following components (dollars in thousands):

	Reorganized XO December 31, 2003	Predecessor XO December 31, 2002
Accrued taxes	$ 49,046	$ 57,649
Accrued compensation	46,124	58,551
Accrued operative expenses	27,837	27,807
Deferred income	26,011	37,109
Accrued telecommunications costs	19,491	28,494
Accrued restructuring	20,046	16,364
Other accrued liabilities	19,798	40,128
	$208,353	$266,102

12. ACCOUNTING FOR ASSET RETIREMENT OBLIGATIONS

The Company leases Internet data center facilities and various technical sites. Terminating and decommissioning these locations would require the removal of any XO assets and restoration of the leased space to its original condition. Accordingly, upon adoption of SFAS No. 143, the Company recorded an estimated asset retirement obligation of $12.0 million, which was estimated using management's best estimate of the expected cash flows. The present value of the asset retirement obligation was calculated using a discount rate of 8.0% over a period of 5-20 years, which is representative of the estimated remaining period XO will occupy its data centers and technical facilities. Accretion expense of $0.8 million for 2003 is included in selling, operating and general expense in the accompanying consolidated statement of operations.

13. LONG-TERM DEBT

The Company has a secured Credit Facility which matures on July 15, 2009. There are no additional borrowings available under the Credit Facility. There are no current debt service requirements since cash interest payments as well as automatic and permanent quarterly reductions on the principal amount outstanding do not commence until 2009. However, in the event that consolidated excess cash flow (as defined in the Credit Facility) for any fiscal quarter during the term of the agreement is greater than $25 million, at the request of the lender, the Company will pay an amount equal to 50% of such excess cash flow greater than $25 million toward the reduction of outstanding indebtedness. In addition, if the ratio of XO's consolidated earnings before interest, taxes, depreciation and amortization to interest expense for the four consecutive quarters exceeds 4:1, XO would be required to pay cash interest, unless waived by the lenders.

The security for the Credit Facility consists of all assets of XO Parent, including the stock of its direct and indirect subsidiaries, and all assets of virtually all of those subsidiaries. The Credit Facility limits additional indebtedness, liens, dividend payments and certain investments and transactions, and contains certain covenants with respect to EBITDA (earnings before interest, taxes, depreciation and amortization) requirements and maximum capital expenditures. The Company was in compliance with these covenants at December 31, 2003. The Company is also required to maintain an unrestricted cash balance of $45 million at December 31, 2003, and $25 million at the end of each fiscal quarter thereafter during the term.

At December 31, 2003, long-term debt of $529.9 million was outstanding on the Credit Facility and $6.9 million of accrued interest that if not paid, converts to principal. At December 31, 2003, more than 90% of the underlying loans of the Credit Facility are held by an entity controlled by Mr. Carl C. Icahn, Chairman of the board of directors ("Mr. Icahn"). As discussed above, the Company is not required to pay cash interest accrued on the principal amount under the Credit Facility until it meets certain financial ratios; however the Company can elect to begin paying interest in cash prior to the required date. Loans under the Credit Facility bear interest, at the Company's option, at an alternate base rate, as defined, or a Eurodollar rate, plus in each case, applicable margins. Once the Company begins to pay accrued interest in cash, the applicable margins are reduced. At December 31, 2003, the annualized weighted average interest rate applicable to outstanding borrowings under the Credit Facility was 7.57%.

14. STOCKHOLDERS' EQUITY

Pursuant to the Company's Certificate of Incorporation that was adopted in connection with the Plan of Reorganization, the Company has the authority to issue 1,000.0 million shares of New Common Stock and 200.0 million shares of new undesignated preferred stock. As of December 31, 2003, approximately 96.3 million shares of New Common Stock had been issued, more than 80% of which were owned by entities controlled by Mr. Icahn.

As discussed in Note 2, XO Parent's pre-petition senior note holders and pre-petition general unsecured creditors were entitled to, among other consideration, warrants to purchase shares up to an additional 23.75 million shares of New Common Stock.

The warrants consist of:

- Series A Warrants to purchase 9.5 million shares of New Common Stock at an exercise price of $6.25 per share;
- Series B Warrants to purchase approximately 7.1 million shares of New Common Stock at an exercise price of $7.50 per share; and

- Series C Warrants to purchase approximately 7.1 million shares of New Common Stock at an exercise price of $10.00 per share.

The warrants were valued at approximately $44.9 million using a Black Scholes model at the Effective Date and are included in reorganized XO's common stock in the accompanying consolidated balance sheet. The warrants will expire 7 years after the date of issuance. The exercise price applicable to each respective series of warrants is subject to adjustment in certain events. Entities controlled by Mr. Icahn own approximately 40% of these warrants as they owned pre-petition senior notes.

In addition to the outstanding warrants discussed above, the Company has a stock option plan that can further dilute investors if exercised. This stock option plan is discussed further in Note 16. On December 31, 2003, there were 2.4 million exercisable stock options.

15. INCOME TAXES

As of December 31, 2003, XO had net operating loss carryforwards of approximately $1.0 billion. All of XO's net operating loss and a substantial amount of XO's capital loss carryforward generated prior to the Bankruptcy Effective Date have been reduced as a result of the discharge and cancellation of various pre-petition liabilities. XO's use of the surviving capital loss carryforward of $0.2 billion is subject to limitations imposed under the ownership change rules in the U.S. Internal Revenue Code. Also, the utilization of the expected tax benefit from property and equipment depreciation could also be impacted by the ownership change rules of the U.S. Internal Revenue Code.

XO will join with the affiliated group of corporations controlled by Mr. Icahn in filing a consolidated federal income tax return for the year ended December 31, 2003. In January 2004, Mr. Icahn's ownership percentage fell below the amount required by the Internal Revenue Code for the filing of consolidated returns. As such, in January 2004, XO deconsolidated with Starfire Holding Corporation ("Starfire"), the Parent entity of the affiliated group of corporations controlled by Mr. Icahn. XO entered into a Tax Allocation Agreement with Starfire which provides that while XO files on a consolidated basis with Starfire, Starfire will pay all consolidated federal income taxes on behalf of the consolidated group that includes XO, and XO will make payments to Starfire in an amount equal to the tax liability, if any, that it would have if it were to file as a consolidated group separate and apart from Starfire. Upon deconsolidation, the Tax Allocation Agreement generally provides that Starfire will reimburse XO each year going forward for the excess of XO's actual income taxes over the income tax that would have been required if NOLs or other tax attributes used by the Starfire consolidated group excluding XO, if any, were available to XO.

Components of deferred tax assets and liabilities were as follows (dollars in thousands):

	Reorganized XO December 31, 2003	Predecessor XO December 31, 2002
Deferred tax assets:		
Provisions not currently deductible	$ 172,368	$ 123,280
Property, equipment and other long-term assets (net)	893,957	367,208
Net operating loss and capital loss carryforwards	483,453	1,863,336
Total deferred tax assets	1,549,778	2,353,824
Valuation allowance	(1,540,612)	(2,028,331)
Net deferred tax assets	9,166	325,493
Deferred tax liabilities:		
Property, equipment and other long-term assets (net)	—	(101,402)
Other identifiable intangibles	(15,997)	(222,537)
Other	—	(1,554)
Total deferred tax liabilities	(15,997)	(325,493)
Net deferred tax liability	$ (6,831)	$ —

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

	Reorganized XO 2003	Predecessor XO 2002
Statutory U.S. federal rate	35.0%	35.0%
State income taxes, net of federal benefit	6.0%	6.0%
Valuation allowance for deferred tax assets	(41.0%)	(18.3%)
Other identifiable intangibles	—	(22.7%)
Effective income tax rate	—%	—%

16. STOCK COMPENSATION ARRANGEMENTS

The XO Communications, Inc. 2002 Stock Incentive Plan ("the 2002 Stock Incentive Plan") was adopted upon the Effective Date. Under the 2002 Stock Incentive Plan, the Company is authorized to issue awards for up to 17.6 million shares of New Common Stock in the form of restricted stock or options to purchase stock. The 2002 Stock Incentive Plan is administered by the Compensation Committee of the Company's Board of Directors, which has the discretionary authority to determine all matters relating to awards of stock options and restricted stock, including the selection of eligible participants, the number of shares of common stock to be subject to each option or restricted stock award, the exercise price of each option, vesting, and all other terms and conditions of awards. Unless the Compensation Committee designates otherwise, all options expire on the earlier of (i) ten years after the date of grant, (ii) twelve months after termination of employment with XO due to death or complete and permanent disability, (iii) immediately upon termination of employment by XO for cause, or (iv) three months after termination of employment by the employee or by XO for other than cause. Upon the Effective Date of the plan of Reorganization, all options under any predecessor XO stock option plans were cancelled and the plans were terminated.

On June 20, 2003, XO filed a registration statement covering the offer and sale of stock options and stock appreciation rights ("SARs") to be granted in conjunction with the 2003 Employee Retention and Incentive Plan (the "Retention Plan") for an aggregate award of 1.9 million shares of New Common Stock. (the "Retention Plan Awards"). Approximately 200,000 options and approximately 10,500 SARs were granted in the third quarter of 2003, fifty percent of which were vested and exercisable on the date of grant, with the remaining fifty percent vesting ratably every month for twenty four months following the month of grant. Additional grants may be made in 2004 if the Company attains certain financial goals in the second half of 2003. The financial goals and the terms of the Retention Plan were established by the Company's Board of Directors. The per share exercise price for the Retention Plan Awards was set at $5.84. Any compensation was recorded as deferred compensation and amortized to on a straight line basis expense based on the associated vesting period.

The following two tables summarize information regarding option activity under the 2002 Stock Option Plan for the year ended December 31, 2003:

	Number of Shares	Weighted Average Exercise Price
Outstanding at the Effective Date	—	$ —
Granted	15,394,162	$5.09
Canceled	(3,697,068)	$5.02
Exercised	(1,274,139)	$5.01
Outstanding at December 31, 2003	10,422,955	$5.12
Exercisable, at December 31, 2003	2,424,903	$5.10

	Options Outstanding			Options Exercisable	
Range of Exercise Prices	Options Outstanding at December 31, 2003	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Options Exercisable at December 31, 2003	Weighted Average Exercise Price
$ 4.80 - $7.05	10,422,955	9.1	$ 5.12	2,424,903	$ 5.10

17. SUPPLEMENTAL DISCLOSURE

Cash flows

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

	Reorganized XO	Predecessor XO	
	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001
Non-cash financing and investing activities were as follows:			
Class A common stock, warrants and options issued in acquisitions and under lease arrangements	$ —	$ —	$ 29,055
Redeemable preferred stock dividends, paid in shares of redeemable preferred stock	—	—	86,237
Accrued redeemable preferred stock dividends, payable in shares of redeemable preferred stock	—	—	6,524
Assumption of preferred stock and liabilities in acquisitions	—	—	8,816
Conversion of 6½% redeemable cumulative preferred stock to Class A common stock	—	35	17,700
Conversion of accrued interest to long-term debt	29,901	—	—
Cash paid for interest	$ 2,315	$11,681	$313,178

Employee Savings and Retirement Plan

At December 31, 2003, the Company had a defined contribution plan, generally covering all full time employees in the United States. The Company provides a match to all eligible employees based on certain plan provisions and the discretion of the Board of Directors. Effective April 1, 2002, the Company changed its employer matching contribution from a 100% matching contribution up to 5% of the participant's compensation to a 50% matching contribution up to 5% of the participant's compensation. Company contributions were $4.8 million, $7.0 million and $12.5 million during 2003, 2002 and 2001, respectively.

18. OPERATING SEGMENTS

Reportable Segments

The Company operates its business as one telecommunications segment. The Company's communications segment includes all of its products and services including data, voice, integrated voice and data, and other services. These services have similar network operations and technology requirements and are sold through similar sales channels to a similar targeted customer base. Therefore, the Company manages these services as a single segment that are sold in geographic areas, or markets, within the United States, or that are sold to customers with a presence across geographical markets.

Products and Services

The Company classifies its products and services revenues offered by its communications services segment into voice services, data services, integrated voice and data services, and other services (dollars in thousands):

	Reorganized XO Year Ended	Predecessor XO Year Ended December 31,	
	2003	2002	2001
Voice services	$ 572,774	$ 659,558	$ 609,885
Data services	392,742	472,247	596,664
Integrated voice and data services	144,967	128,048	52,018
Total revenue	$1,110,483	$1,259,853	$1,258,567

19. SELECTED QUARTERLY DATA (Unaudited)

Quarterly financial information is summarized in the table below (dollars in thousands, except per share data):

	Reorganized XO Quarter ended 2002			
	March 31,	June 30,	September 30,	December 31,
Revenue	$286,093	$283,918	$279,433	$261,039
Cost of service	107,506	104,898	106,935	102,790
Loss from operations	(14,015)	(13,260)	(35,878)	(48,705)
Net loss (a)	(20,488)	(19,836)	(40,787)	(21,443)
Net loss per common share (basic and diluted) (a) (d)	(0.22)	(0.21)	(0.42)	(0.22)
	Predecessor XO Quarter ended 2002			
	March 31,	**June 30,**	**September 30,**	**December 31,**
Revenue	$ 333,405	$ 325,480	$ 301,526	$ 299,442
Cost of service	140,367	134,346	126,215	121,996
Loss from operations (b)	(182,663)	(176,771)	(673,001)	(176,463)
Net loss before cumulative effect of accounting change	(299,028)	(346,133)	(695,209)	(169,822)
Net loss (c)	(2,175,654)	(346,133)	(695,209)	(169,822)
Net loss applicable to common shares	(2,198,480)	(286,851)	(695,209)	(169,822)
Net loss per common share (basic and diluted) (c) (d)	(4.97)	(0.65)	(1.57)	(0.39)

a. Fourth quarter of 2003 includes a $33.5 million realized investment gain.

b. In the third quarter of 2002, loss from operations includes a non-cash asset write down totaling $477.3 million.

c. In the first quarter of 2002, net loss includes a $1,876.6 million impairment charge to write-off all of XO's goodwill as a cumulative effect of accounting change, pursuant to SFAS No. 142.

d. For the year 2003, the net loss per share data has been calculated based on the shares outstanding subsequent to consummation of the Plan of Reorganization. For the year 2002, the net loss per share data has been calculated based on the shares outstanding of the Company's pre-petition class A and class B common stock prior to the consummation of its Plan of Reorganization.

20. RELATED PARTY TRANSACTIONS

Various entities controlled by Mr. Icahn hold the following interests in XO:

	Outstanding Common Stock	Series A, B and C Warrants	Credit Facility
	(unaudited)	(unaudited)	(unaudited)
At December 31, 2003	Greater than 80%	Greater than 40%	Greater than 90%
At January 31, 2004	Greater than 60%	Greater than 40%	Greater than 90%

In addition, entities controlled by Mr. Icahn have acquired an option to purchase 6.25 million additional shares of XO's New Common Stock from Franklin Mutual Advisors, LLC at a strike price of $4.25 per share which expires June 21, 2004. After closing the Rights Offering in January 2004, Mr. Icahn's ownership interest in our outstanding common stock was reduced to over 60% (unaudited).

As a result of his majority ownership, Mr. Icahn can elect all of our directors, appoint the members of the committees of our Board of Directors, appoint key members of our executive management team, and appoint our auditors. Currently, Mr. Icahn is Chairman of the Board of Directors and three employees of Icahn Associates sit on the Board of Directors and various Committees of the Board of Directors. Under applicable law and XO's Certificate of Incorporation and by-laws, certain action cannot be taken without the approval of holders of a majority of our voting stock, including, without limitation, mergers, acquisitions, the sale of substantially all our assets, and amendments to our Certificate of Incorporation and by-laws.

Mr. Icahn, through various entities that he owns or controls, has the right to require XO to register, under the Securities Act of 1933, shares of New Common Stock held by such entities and to include shares of New Common Stock held by them in certain registration statements filed by XO, pursuant to a Registration Rights Agreement approved by the Bankruptcy Court in connection with XO Parent's Chapter 11 proceedings.

In February 2003, Dixon Properties, LLC ("Dixon"), which is controlled by Mr. Icahn, acquired ownership of the building in which XO headquarters is located in a transaction that was approved by the Bankruptcy Court. XO currently leases approximately 170,000 square feet of space in that building. Pursuant to the assumed lease agreement, XO has paid $3.3 million in lease expense to Dixon for the year ended December 31, 2003 and XO is obligated to pay approximately $15.6 million to Dixon through the expiration of the initial term of the lease, which is November 30, 2007.

XO has entered into a Tax Allocation Agreement, dated January 16, 2003, between XO and Starfire Holding Corporation ("Starfire"), the parent entity of the affiliated group of corporations controlled by Mr. Icahn. XO and Starfire intend to file consolidated returns during the period in which Mr. Icahn's ownership of XO is equal to or greater than 80%, as required by the Internal Revenue Code. The Tax Allocation Agreement provides that Starfire will pay all consolidated federal income taxes on behalf of the Icahn consolidated group that includes XO, and XO will make payments to Starfire in an amount equal to the tax liability, if any, that it would have incurred if it were to file its own consolidated return separate and apart from Starfire. Upon the closing of the Rights Offering in January 2004, Mr. Icahn ownership percentage fell below 80% (unaudited). Consequently XO will no longer file as part of Icahn's consolidated group after January 2004. Upon deconsolidation, the Tax Allocation Agreement generally provides that Starfire will reimburse XO each year going forward for the excess of XO's actual income tax expense over the income tax that would have been owed if the net operating losses or other tax attributes used in prior periods by the Starfire consolidated group excluding XO, if any, were still available to XO.

The Company provides certain telecommunications services to companies affiliated with Mr. Icahn. For the year ended December 31, 2003, the total revenue recognized on such services affiliated with Mr. Icahn was approximately $0.4 million. The Company has purchased approximately $0.3 million in services from Icahn affiliates during 2003. During 2003, XO purchased approximately $1.1 million in hardware and services from Dell Computers, Inc. Mr. Adam Dell, an XO director, is Mr. Michael Dell's, the Chief Executive Officer of Dell Computers, brother.

21. COMMITMENTS AND CONTINGENCIES

Operating Commitments

The Company is leasing premises under various noncancelable operating leases for administrative space, building access, and other 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 2029. The Company also has various noncancelable long-term contractual obligations associated with maintenance and service agreements.

Future minimum lease commitments required under noncancelable operating leases and contractual obligations are as follows (dollars in thousands):

Year Ending December 31,	Operating lease obligations	Other long-term contractual obligations
2004	$ 60,623	$ 53,974
2005	57,974	33,768
2006	53,269	24,484
2007	49,159	23,451
2008	38,823	23,048
Thereafter	188,084	96,811
Total minimum commitments	$447,932	$255,536

Rent expense for cancelable and noncancelable leases totaled approximately $54.0 million, $76.4 million, and $100.0 million for the years ended December 31, 2003, 2002, and 2001, respectively. The minimum lease payments noted above have not been reduced for sublease income totaling approximately $6.1 million at December 31, 2003.

Capital Leases

Network assets under capital leases totaled approximately $1.4 million and $16.3 million as of December 31, 2003 and 2002, respectively, and are included in telecommunications networks in property and equipment. Depreciation on leased assets of $0.4 million and $2.0 million for the years ended

December 31, 2003 and 2002, respectively, is included in depreciation expense. Future minimum lease payments under capital lease obligations as of December 31, 2003 are as follows (dollars in thousands):

Year Ending December 31,	
2004	$2,809
2005	2,668
2006	2,416
2007	1,733
2008	277
Thereafter	—
Total minimum capital lease payments	9,903
Less: imputed interest	(2,722)
Less: current portion of capital lease obligations	(1,660)
Long-term portion of capital lease obligation	$5,521

The Company provides intercity transport primarily through five year leases of wavelength capacity that are paid for at the beginning of the term. The first of these leases expires in 2006. At that time, XO will either renew these leases or light its intercity fiber network, either of which will be a substantial capital expenditure.

Legal Proceedings

XO is involved in lawsuits, claims, investigations and proceedings consisting of commercial, securities, tort, and employment matters, which arise in the ordinary course of business. In addition, disputes with respect to general unsecured claims and two administrative expense claims against XO Parent in the aggregate amount of approximately $23.0 million remain pending from the XO Parent Chapter 11 proceedings. In accordance with SFAS No. 5, "Accounting for Contingencies," XO makes a provision for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. XO believes it has adequate provisions for any such matters. XO reviews these provisions at least quarterly and adjusts these provisions to reflect the impacts of negotiations, settlements, rulings, advice of legal counsel, and other information and events pertaining to a particular case. Litigation is inherently unpredictable. However, XO believes that it has valid defenses with respect to legal matters pending against it. Nevertheless, it is possible that cash flows or results of operations could be materially affected in any particular period by the unfavorable resolution of one or more of these contingencies.

Unfunded Affiliate Pension Obligation (Unaudited)

As affiliates of Mr. Icahn held over 80% of the outstanding New Common Stock of XO Parent at December 31, 2003, applicable pension and tax laws made each member of a plan sponsor's "controlled group" (generally defined as entities in which there is at least an 80% common ownership interest) jointly and severally liable for certain pension plan obligations of the plan sponsor. These pension obligations include ongoing contributions to fund the plan, as well as liability for any unfunded liabilities that may exist at the time the plan is terminated. In addition, the failure to pay these pension obligations when due may result in the creation of liens in favor of the pension plan or the Pension Benefit Guaranty Corporation, (the "PBGC") against the assets of each member of the plan sponsor's controlled group.

As a result of the reduction to less than 80% ownership interest in XO Parent by Mr. Icahn's affiliates after the Rights Offering, XO Parent and its subsidiaries will no longer be subject to the pension liabilities of any entities in which Mr. Icahn has a direct or indirect ownership interest of at least 80%.

22. SUBSEQUENT EVENTS (Unaudited)

Acquisition of Assets of Allegiance Telecom, Inc.

On February 19, 2004, the United States Bankruptcy Court for the Southern District of New York approved the Asset Purchase Agreement by and between XO Parent and Allegiance Telecom, Inc., or ("Allegiance"), pursuant to which XO Parent has agreed to acquire substantially all of the assets of Allegiance for approximately $311.0 million in cash and approximately 45.4 million shares of New Common Stock. Governmental approval should occur prior to, or shortly after the second quarter of 2004. At that point in time, the two companies will operate under a management agreement whereby the combined management team will exercise day to day operating control over the assets and operations to be acquired from Allegiance. The acquisition of the Allegiance assets should be consummated during the third quarter of 2004 after all other federal and state regulatory approvals are obtained. While the Company believes the approvals will be forthcoming, there can be no assurance that XO will obtain the governmental approvals and clearances required to consummate the acquisition of the Allegiance assets.

The Allegiance assets consist primarily of:

- switching and routing equipment, located both in current Allegiance facilities and in facilities operating by one or more incumbent local exchange carriers;
- physical points of presence in the form of network operations centers, data centers, central offices, and sales offices located in 36 major metropolitan areas;
- customer and sales agreements that constitute a majority of Allegiance's voice and data revenues;
- leased intercity and metro fiber network capacity that is both redundant to and expansive of XO's current network; and
- billing, provisioning, and other back-office information technology platforms.

Rights Offering

As part of its Plan of Reorganization, XO Parent agreed to initiate a Rights Offering that allowed certain holders of claims and interests in XO Parent as of the November 15, 2002 record date to subscribe for up to 40.0 million shares of New Common Stack at $5.00 per share. The Rights Offering closed on January 5, 2004. An aggregate of 39.7 million shares were issued, yielding net proceeds of $197.6 million. The proceeds were used to reduce its outstanding debt and accrued interest under the Credit Facility from $536.8 million to $339.2. See also Note 2.

XO Communications, Inc.

Schedule II — Consolidated Valuation and Qualifying Accounts
For The Years Ended December 31, 2003, 2002 and 2001

Predecessor XO

(dollars in thousands)	Beginning Balance	Additions charged to expense	Reductions	Balance Ending
Allowance for doubtful accounts				
2001	$ 20,999	$ 45,757	$ (34,264)	$ 32,492
2002	$ 32,492	$ 53,631	$ (49,093)	$ 37,030
Restructuring accrual				
2001 (a)	$ —	$509,202	$(383,429)	$125,773
2002 (b)	$125,773	$480,168	$(526,951)	$ 78,990

(a) Only $16.6 million of the reduction in the 2001 restructuring accrual was for cash payments. The balance was associated with the write down for the excess of carrying value of assets to be sold or abandoned and was applied to those assets.

(b) Only $49.7 million of the reduction in 2002 restructuring accrual was for cash payments. The balance was associated with the non-cash asset write down resulting from an agreement with Level 3 to amend various agreements relating to XO's Level 3 intercity fiber network facilities.

Reorganized XO

(dollars in thousands)	Beginning Balance	Reorganization Adjustments	Additions charged to expense	Reductions	Ending Balance
Allowance for doubtful accounts					
2003	$37,030	$ —	$29,998	$(34,042)	$32,986
Restructuring accrual					
2003 (c)	$38,725	$26,809	$11,618	$(17,176)	$59,976

(c) The beginning balance was reduced to its net present value when we implemented fresh start.

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2004

OR

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

Commission File No. 0-30900

XO COMMUNICATIONS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**54-1983517**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. employer identification no.)**

11111 Sunset Hills Road
Reston, Virginia 20190
(Address of principal executive offices, including zip code)

(703) 547-2000
(Registrant's telephone number, including area code)

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

Securities registered pursuant to Section 12(g) of the Act:
Common Stock, par value $0.01 per share
(Title of class)

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 ☑ No ☐

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

Indicate by check mark whether the Registrant is an accelerated filer (as defined by Rule 12b-2 of the Act.). Yes ☑ No ☐

The aggregate market value of the common stock held by non-affiliates of the Registrant, based upon the closing sale price of the common stock on June 30, 2004 (which is the last business day of the Registrant's second fiscal quarter), as reported on the NASDAQ Over-the-Counter Bulletin Board, was approximately $375.7 million. Shares of common stock held by each executive officer and director and by certain persons who own 5% or more of the outstanding 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.

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13, or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. YES ☑ No ☐

Number of shares of common stock outstanding as of March 14, 2005: 181,933,035

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement to be issued in conjunction with registrant's annual stockholders' meeting to be held on May 9, 2005 are incorporated in Part III.

TABLE OF CONTENTS

PART I

Item 1. Business

This document contains certain "forward-looking statements," within the meaning of the Private Securities Litigation Reform Act of 1995, including statements regarding, among other items, our expected financial position, business, and financing plans. These forward-looking statements are based on our current expectations and are naturally subject to risks, uncertainties, and changes in circumstances, certain of which are beyond our control. Actual results may differ materially from those expressed or implied by such forward-looking statements.

The words "believe," "plan," "target," "expect," "intends," and "anticipate," and expressions of similar substance identify forward-looking statements. Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that those expectations will prove to be correct. Important factors that could cause actual results to differ materially from the expectations described in this report are set forth under "Risk Factors" in Item 1 and elsewhere in this report. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of their dates. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

Business Overview

XO Communications, Inc., or XO, a Delaware corporation, is a leading facilities-based, competitive telecommunications services provider that delivers a comprehensive array of telecommunications services to business customers. We provide our services, including local and long distance voice, Internet access, private data networking and hosting services, through our national telecommunications network, which consists of more than 6,700 metro route miles of fiber optic lines connecting 953 unique ILEC end-office collocations in 37 U.S. cities. In addition, we own licenses to deliver telecommunications services via local, multipoint distribution service, or LMDS, wireless spectrum in all of the largest U.S. cities. We market our services primarily to business customers, ranging from small and medium businesses to Fortune 500 companies to carrier and wholesale customers. Our services offer an effective telecommunications solution for nearly any business, and our national telecommunications network is particularly advantageous to multi-location businesses that desire to improve communications among their locations, whether within a single metropolitan area or across the country.

2004 Highlights

- *Acquisition of Allegiance Telecom, Inc.* We acquired the telecommunications services assets of Allegiance Telecom, Inc. on June 23, 2004. The acquisition of Allegiance substantially expanded our local facilities, and significantly increased the number of business customers to which we can cost-effectively provide service. We completely integrated their administrative functions and have achieved all of the originally estimated $100 million of annualized selling, operating and general synergies. We have made substantial progress in achieving the originally estimated $60 million of annualized network synergies.
- *Positive Cash Flow from Operations for 2004.* We generated positive cash flow from operations (excluding capital expenditures) in 2004, marking the third consecutive fiscal year that we have achieved that operating milestone.
- *Raised $200 million of Capital.* In August 2004, we strengthened our balance sheet by raising an additional $200 million in capital to support our ongoing operations and to fund potential acquisitions 95% of which came from our significant shareholder.

The U.S. Telecommunications Market

While competitive local exchange carriers, or CLECs, like us have provided telecommunications competition and service since 1996, the market for telecommunications services, particularly local exchange services, remains dominated by the incumbent telecommunications carriers or ILECs, consisting primarily of the former subsidiaries of AT&T known as the Regional Bell Operating Companies, or RBOCs, — Verizon, SBC Communications, Qwest Communications, and BellSouth — which each own substantially the entire local exchange network in their respective operating regions of the United States.

Aggregate revenue earned from the sale of wired telecommunications services in 2004 has been estimated at approximately $225 billion, down approximately three percent from 2003. Telecommunications sales to business customers, however, is estimated to have remained relatively constant at $91 billion, with sales of local exchange services estimated to have increased by approximately one percent to approximately $42.5 billion in 2004 compared to 2003. Telecommunications spending by businesses who spend less than $10,000 per month, or small and medium businesses, was estimated to be $75 billion in 2004.

The telecommunications industry currently remains in a state of competitive transition. The telecommunications services market has remained focused on pricing and many telecommunications providers have continued to face significant competitive pressure to reduce prices. Also, the combination of new federal and state regulations, emergence of new technologies, industry consolidation, growth of the mobile wireless market, and entry of new telecommunications competitors has contributed to a rapidly changing market for telecommunications services. These issues and the potential impact to XO are discussed below.

Recent Federal Rulemaking. Effective as of March 11, 2005, the Federal Communications Commission's, or FCC's, Triennial Review Remand Order, or TRRO, altered a number of significant federal regulations applicable to the provision of competitive telecommunications services in a manner favorable to incumbent carriers. The TRRO established new standards for when CLECs obtain cost-based rates from ILECs when leasing unbundled network elements, or UNEs, which connect a customer's location with the applicable communications network end office, commonly referred to as "loops". This aspect of the TRRO will result in an increase to our overall costs of service in 2005.

The TRRO also curtailed the ability of CLECs to obtain cost-based UNE rates for network elements linking central offices in which they have located their own equipment, but between which they do not own proprietary fiber lines. Fiber lines between central offices is referred to in our industry as "local transport". This aspect of the TRRO will not have a material impact on us as we own or lease under long-term agreements nearly all of the local transport that we use to connect central offices in which we own equipment. This aspect of the TRRO could, however present opportunities for us to sell our own network capacity to telecommunications companies that are negatively impacted by the TRRO ruling on local transport.

The TRRO also severely curtailed the ability of CLECs to lease switching capacity from ILECs at cost-based rates, which practice is known in the telecommunications industry as unbundled network element platform, or UNE-P. We are not materially impacted by this aspect of the TRRO as we own all of the switching facilities we use in our business. We anticipate that one of the results of the TRRO will be that many CLECs that are substantially dependent on UNE-P will need to either acquire their own switches, seek a facilities-based partner to switch their customers' traffic, or find other strategic alternatives to their current business models. One possible result of the TRRO on UNE-P dependent carriers is additional consolidation of existing telecommunications carriers.

Emergence of New Technologies. Several new technologies are being adopted by telecommunications carriers that could cause significant changes in the competitive landscape for telecommunications services. Such technologies include:

- **IP Communications.** Voice over Internet Protocol, or VoIP, technology enables delivery of voice and data telecommunications services over a single Internet Protocol or IP network, rather than through the existing Public Switched Telephone Network or PSTN. XO's experience and network architecture allows us to take advantage of the development of VoIP services. XO's initial VoIP implementation, named XOptions Flex, enables customers to utilize "dynamic bandwidth allocation" to maximize the utilization of their bandwidth by allocating it for data applications during periods when voice lines are idle. XO also anticipates that it will add additional IP-enabled features to its existing products.

- **Fixed Broadband Wireless.** With the exception of building locations to which we have constructed our own fiber or network connections, we are dependent upon the ILECs for obtaining network access to our customers' buildings, which access is referred to in our industry as "last mile" connectivity. There has been ongoing development of technical equipment and data encryption and compression protocols that permit the use of high bandwidth wireless connections between physical locations that are located within a line of sight across relatively short distances, usually under five miles. This fixed wireless, point-to-point connectivity may, in limited circumstances, allow us to obtain direct network access to our customers' buildings via wireless connection without the requirement of leasing network access from the ILECs.

- **Mobile Wireless Technologies.** Wireless carriers have engaged in rapid development of new high bandwidth applications to be delivered to their customers via wireless devices, commonly referred to as "3G" broadband wireless networks. Such applications include the delivery of video and photos via wireless connection. The ongoing adoption of broadband networks and applications could mean that current wireless telecommunications carriers will require significantly greater wireline bandwidth for transport of their customers' traffic, presenting an opportunity for facilities based carriers such as XO to offer transport and termination services to those wireless carriers.

Industry Consolidation. On January 31, 2005, SBC Communications, Inc. and AT&T Corp. announced their intention to enter into a business combination. In February 2005, Verizon Communications, Inc. and MCI, Inc. announced and agreement to enter into a business combination, and Qwest Communications International, Inc. announced a bid to compete with Verizon's purchase offer. Such transactions, if consummated, would result in substantial consolidation of U.S. wireline telecommunications resources and revenue. In addition, as reflected in our acquisition of the CLEC businesses of Allegiance Telecom, Inc. and the acquisitions of Cable and Wireless USA, Inc. by Savvis Communications, Inc., Focal Communications, Inc. by Broadwing Corporation, and KMC Telecom Corp. by CenturyTel, Inc., substantial consolidation has also taken place among CLECs. Assuming that each of the announced transactions involving AT&T and MCI occur as planned, market power for U.S. telecommunications services will be further consolidated among the ILECs, and both business and residential consumer choice will be significantly reduced. While it is not certain what the effects of this industry consolidation will be, we believe that one possible result could be that prices for telecommunications services would stabilize due to reduced competition.

Growth of the Mobile Wireless Market. Unlike the market for wireline telecommunications services, the overall market for mobile wireless telecommunications services has continued to grow in recent years. While some of our target business customers have supplemented their existing wireline telecommunications infrastructure with mobile wireless communications services, we believe that business customers will generally continue to require wireline services that we provide because of the bandwidth limits of mobile wireless services and the current lower costs of wireline telecommunications services.

Entry of New Telecommunications Competitors. In recent years, new competitors have emerged to traditional, facilities-based telecommunications services providers. Among these new competitors are VoIP providers, including companies such as Vonage and Covad, and providers of other forms of media or telecommunications services, including cable companies such as Comcast and Cox Communications. The FCC has noted in several public comments that it expects that such competitors will provide significant competition to the ILECs in the future. While such companies are likely to experience growth in their telecommunications services businesses in the future, we believe that we will not compete directly with these competitors as they are focused primarily on residential, and, to a lesser extent, small business customers.

Competitive Strategy

We are executing on our strategic plan by focusing on the five key strategic elements below.

In addition, we are also retaining investment bankers and consultants who will develop and make recommendations to us regarding our strategic alternatives.

Leverage National Network Footprint. Our primary competitive strategy is to leverage the national reach and technological sophistication of our metro and intercity fiber network. We maintain a national network that includes 953 collocations from which we have the capability to serve over 70 U.S. markets. We believe that our network footprint gives us the network capability to provide approximately 45% of all telecommunication services revenue from U.S. small to medium businesses, or SMBs. Our national network can also reach markets and customers that no single ILEC is currently capable of serving over its own regional network, and we are among a small number of CLECs with national capabilities. Consequently, we believe that our national network has capabilities that appeal to business customers in a manner that cannot currently be duplicated by any of the ILECs, and our national reach allows us to market to a significant portion of the total market for business telecommunications services.

Our network includes an OC-192 IP backbone with extensive cross connections between the Internet and the public switched telephone network, or PSTN, enabling us to accept IP packets of data originated or carried over the Internet, and convert that information to voice traffic terminated or switched over the traditional PSTN. We believe that the interoperability of our network for both PSTN and IP traffic will allow carrier and wholesale customers to access our network more flexibly, and enable us to offer services with significant appeal to carrier and wholesale customers.

Focus on Business Customers. XO's services include a broad portfolio across voice, data and integrated bundled offerings tailored for the business customer. Although we have both small customers with limited telecommunications needs and large telecommunications carrier/wholesale customers, our predominant focus is SMBs.

Focus on Profitable Revenue. We monitor our sales and provisioning systems to maintain and increase the profitability of the telecommunications services that we provide. In addition, we have implemented provisioning rules that, based on geography and the location of our network facilities, allow us to measure at the time of sale whether a prospective sale will be profitable to us.

Diverse Service Offerings. We offer a broad portfolio of voice, data and integrated services to business customers. Our core integrated SMB service offerings deliver simplicity of use and billing. Although we believe that wireline telecommunications revenues have been in decline among mature telecommunications carriers in general, we have experienced slight increases in sales of our data and enhanced products and features that add value for our SMB customers. We continue to introduce new products and will launch the first in a series of planned VoIP services, including XOptionsFlex, in 2005.

Strategic Acquisitions. We actively consider strategic merger and acquisition opportunities that are likely to result in increased revenue and reduced costs of service by, among other things, expanding our network, allowing us to optimize our network assets, expanding our service portfolio, or expanding our customer base. We believe that such merger and acquisition opportunities will arise in the telecommunications industry in 2005 generally as a result of regulatory developments, technological developments and shifting marketplace pressures.

Our Services

We provide business customers with a comprehensive array of voice and data telecommunications services, including local and long distance voice, Internet access, private data networking and hosting services. We have designed these telecommunications services principally to meet the needs of our business customers, from SMBs to multi-location businesses, large enterprises, as well as carrier and wholesale service providers.

Integrated Voice and Data Services

XOptions and Total Communications. We offer integrated bundled packages of voice and data services, known as XOptions and Total Communications, to SMBs that include flat-rate packages for specified amounts of certain services, including local and long distance voice services, Internet access and web hosting services. Both of these bundled services include a variety of service options designed to accommodate different customers with anywhere from 10 to 100 employees per location. These services can result in significant savings over the average cost of buying these services from separate competitive voice and data providers. We also offer Integrated Access Services, which can reduce SMB's telecommunications costs by combining local voice, long distance, and dedicated Internet access on a single facility.

IP Communications Services. Utilizing our IP backbone, and related IP equipment and software, XO anticipates the introduction of a broad IP-based portfolio that caters to SMBs as well as larger companies that may choose either a hosted or premise-based IP Telephony solution. XO's first planned service to be marketed in 2005, which will be named XOptions Flex, is a solution for SMBs that features dynamic bandwidth allocation, unlimited local and long distance calling, as well as a web-based portal for use by customers in making changes to the use of the product.

Managed Services. We also provide managed services, including shared tenant services, which are telecommunications management services provided to groups of businesses located in the same office building. Managed services enable SMBs to benefit from the efficiencies, including volume discounts, normally available only to larger enterprises. We install a telecommunications system throughout each building we serve, leasing space for on-site sales and service, and offer tenants products and services such as telephones, voice mail, local calling lines, long distance and high-speed Internet connections, all on a single invoice.

Voice Services

Local and Long Distance Voice Services

We offer a variety of voice applications and services as an alternative to the ILECs. These voice services include:

- local standard dial tone, including touch-tone dialing, 911 access and operator assisted calling;
- local multi-trunk dial tone services, including primary rate interface, or PRI, with direct inward dialing, and direct outward dialing;
- long distance services, including 1+, toll free, calling card and operator services;
- IP termination services;
- voice messaging with personalized greetings, send, transfer, reply and remote retrieval capabilities;
- conferencing services, including voice and web conferencing services;
- directory listings and assistance; and
- hosted interactive voice response services.

In each of our markets, we have negotiated and entered into interconnection agreements with the applicable ILEC and certain independent carriers, and implemented permanent local number portability, which allows our new customers to retain their telephone numbers when they choose XO as their service provider.

Data Services

Internet Access

Our Internet access offerings include dedicated access services targeted at businesses that desire single or multipoint high-speed, dedicated connections to the Internet. Our dedicated Internet access service provides guaranteed internet speeds ranging from 56 kilobits per second, or kbps, to 1 Gigabit per second, or Gbps. Our digital subscriber line, or DSL, service also includes a wide range of dedicated access speeds for SMBs. We are a tier-1 Internet backbone provider in the U.S., with over 200 public and private peering arrangements with other Internet backbone networks.

Private Data Networking

We provide dedicated transmission capacity on our networks to customers that desire high-bandwidth data links between locations. We offer special access and point-to-point circuits to telecommunications carriers and other high volume customers, which they use as both primary and back-up circuits. In addition, fiber optic technology that enables signals to be transmitted at different wavelengths on a single fiber allows us to lease one or more dedicated wavelengths to customers that desire high-bandwidth links between locations. We currently offer these services with connections of up to 9.6 gigabits per second, a transmission rate that is described in our industry as OC-192. This service supports a variety of transmission protocols, including Asynchronous Transfer Mode, or ATM, Frame Relay, and Synchronous Optical Network, or SONET.

Our virtual private network, or VPN, services enable customers to deploy tailored, IP-based business applications for secure internal enterprise, business-to-business and business-to-customer data communications among geographically dispersed locations, while also affording high-speed access to the Internet. VPN services also provide secure access for remote users, such as traveling employees and employees working from home or a remote location, which is not possible using private line and frame relay services. We also offer managed firewall services.

Finally, we offer a suite of Ethernet services, including Gigabit Ethernet, or GigE, in most of our U.S. markets, as well as intercity Ethernet services between our markets. Our Ethernet services are designed to provide high-speed, high-capacity connections between customers' local area networks, or LANs, within and between metropolitan areas, which reduces their costs as it eliminates the need for ongoing configuration, management and acquisition of equipment by the customer.

Hosting Services

We offer a range of applications hosting services that can manage a customer's web-based infrastructure and operational needs, allowing customers to focus on their web-based content. In addition, we provide server management tools and services to manage customers' larger computers, which are known as servers, for them.

Our hosting services include:

- *Web Hosting:* support for customers' websites, including design, maintenance and telecommunications services; and
- *Server Collocation:* collocation of customers' servers in our data centers.

We also offer a variety of value-added tools and applications that enable our customers to conduct targeted email marketing, register their web site with hundreds of Internet search engines and directories, build catalogues and sell products over the web, and coordinate meetings and appointments online. And finally, we offer a suite of hosting outsourcing services that provides customers web-based access to email, group distribution lists, calendaring, contacts databases management and file sharing.

Our Network

Our network consists of state of the art metro fiber rings and intercity network capable of carrying high volumes of data, voice, video and Internet traffic. We utilize network assets located across the United States, substantially all of which we own or control through indefeasible exclusive rights or other leasing or contractual arrangements, making us a national facilities-based carrier. We are able to provide our services to our customers entirely over an integrated national network, from the initiation of the voice or data transmission to the point of termination. This allows XO to offer our customers high quality of service and a high level of service.

Metro Fiber Networks and Local Facilities

Our metro fiber networks consist of rings of more than 888,000 fiber miles of fiber optic cables encircling the central business districts of numerous metropolitan areas. A "fiber mile" is equal to the number of route miles multiplied by the number of fibers along that path. We operate 37 metro fiber networks in 22 states and the District of Columbia, including 25 of the 30 largest metropolitan areas in the U.S. In the aggregate, our metro fiber networks connect approximately 953 unique ILEC end-office collocations.

The core of each of our metro fiber networks is a ring of fiber optic cable in a city's central business district that connects to our central offices from which we can provision services to our customers. These central offices contain the switches and routers that direct data and voice traffic to their destinations, and also have the space to house the additional equipment necessary for future telecommunications services. A critical element of our metro fiber network is the number of central offices in which we have located our routing and transmission equipment within each of our local markets, referred to as collocations. In general, a CLEC is able to provision services at lower cost if it operates a collocation within a relatively short distance of its customer. Following our acquisition of the telecommunications assets of Allegiance Telecom, Inc. in June 2004, we operate collocations in 953 central offices as part of our network, virtually all of which are concentrated in the business districts in which our target customers are located. We operate one of the most extensive collocation footprints in the United States. We believe that our extensive collocations provide us with substantial market opportunities to both sell services to our targeted SMB customers and to service as points of termination for traffic originated by other carriers.

Whenever we can, we build and own these metro fiber networks ourselves or obtain indefeasible rights to use fiber so that we can control the design and technology used to best meet our customers' needs. We built our high capacity metro fiber networks using a backbone density typically ranging between 72 and 432 strands of fiber optic cable. Fiber optic cables have the capacity, or bandwidth, to carry tens of thousands of times the amount of traffic as traditionally-configured copper wire. Our high-count fiber strands allow us to augment the scale of our broadband and voice services without incurring significant additional construction costs. Indefeasible exclusive rights are contracts with the owners of fiber optic cables that allow us to use a specified amount of capacity on a specified fiber on those cables for terms ranging from 10 to 25 years.

We operate 37 metro fiber networks serving over 70 markets noted below:

State	Metro Fiber Network Location	Service Market
AZ	Phoenix	Phoenix
CA	Los Angeles	Los Angeles
CA	Orange County	Anaheim
		Costa Mesa
		Fullerton
		Garden Grove
		Huntington Beach
		Inglewood
		Irving
		Long Beach
		Orange
		Santa Ana
CA	Sacramento	Sacramento
CA	San Diego	San Diego
CA	San Francisco	San Francisco
		Oakland
CA	San Francisco (cont)	Fremont
		Milpitas
		Mountain View
		Palo Alto
		Santa Clara
		Sunnyvale
CA	San Jose	San Jose
CO	Denver	Denver
		Boulder-Longmont
DC/VA	Washington DC/ No VA	Washington, DC-MD-VA-WV
FL	Ft Lauderdale	Ft Lauderdale
FL	Miami	Miami
		West Palm Beach-Boca Raton
FL	Orlando	Orlando
FL	Tampa	Tampa-St. Petersburg- Clearwater
GA	Atlanta	Atlanta
		Marietta
IL	Chicago	Chicago
MA	Boston	Boston, MA-NH
		Brockton
		Lawrence, MA-NH
		Lowell, MA-NH
		Worcester, MA-CT
MD	Baltimore	Baltimore
MI	Detroit	Detroit
MN	Minneapolis	Greater Minneapolis/ St. Paul
MO	St Louis	St Louis
NJ	New Jersey	Bergen/ Passaic
		Middlesex-Somerset-Hunterdon
		Newark
		Jersey City
		Monmouth-Ocean
		Trenton
NV	Las Vegas	Las Vegas
NY	New York	Manhattan
		Nassau-Suffolk
OH	Cleveland/ Akron	Cleveland-Lorain-Elyria
		Akron
		Canton-Massillon
OH	Columbus	Columbus
OR	Portland	Portland-Vancouver, OR-WA
PA/ DE	Central PA	Allentown-Bethlehem-Easton
		Harrisburg-Lebanon-Carlisle
		Lancaster
		Reading
		Scranton-Wilkes-Barre-Hazleton
		York
		Wilmington-Newark, DE-MD
		Dover
PA	Philadelphia	Philadelphia, PA-NJ
TN	Memphis	Memphis, TN-AR-MS
TN	Nashville	Nashville
TX	Austin	Austin-San Marco
TX	Dallas/ Ft Worth	Dallas
		Fort Worth-Arlington
TX	Houston	Houston
TX	San Antonio	San Antonio
UT	Salt Lake City	Salt Lake City-Ogden
		Orem/Provo
WA	Seattle	Seattle-Bellevue-Everett
WA	Spokane	Spokane
		Lewiston

Clarkston
Coeur d'Alene

Intercity Network

Our metro fiber networks are connected by our own switching, routing and optical equipment to dedicated, high-capacity wavelengths of transmission capacity, on intercity fiber optic cables, which we refer to as wavelengths and which composes the majority of our over 290,000 intercity fiber miles of network. By using our own switching and routing equipment, we maximize the capacity and enhance the performance of our intercity network as needed to meet our customers' current and future telecommunications needs.

XO has designed and built an advanced and reliable intercity network. There are at least two physically diverse fiber lines connecting each of our markets to any other of our markets. This allows us to reroute traffic around fiber cuts to ensure end-to-end connectivity to our customers. Each metro fiber ring is also connected to our other rings at a minimum of two points. This ensures that customer traffic can be rerouted around any given market to avoid network problems like facility congestion. This also ensures that any problem in a given market will not significantly affect the rest of the network.

Our SONET IP architecture provides the highest level of restoration available today over 10 Gbps wavelengths. Redundant routes and capacity are identified and reserved so that in the event of a failure, the network will systematically restore traffic in the shortest time possible without the need for human involvement.

We prepaid to lease wavelengths, primarily from Level 3 Communications, Inc., or Level 3, for five year periods. The leases for our intercity wavelength capacity will expire in 2006 and 2007. Given the level of traffic in relationship to capacity and the availability of wavelength capacity that was available to us at cost-efficient lease rates, to date, it has generally been more cost-effective to lease wavelengths rather than deploy our own equipment to activate segments of our intercity fiber network, which is discussed below. However, we have designed and installed much of the equipment we use to route traffic so that we can easily transfer voice and data traffic from leased wavelength capacity onto our intercity fiber network as increased traffic on certain segments makes that the more cost effective approach. We expect to either renew the wavelength leases for this capacity, lease the capacity from another vendor, or light our intercity fiber network. Based on the most cost effective option per segment, the current estimate to execute these different options ranges from $25 million to $40 million, although we believe that through the development of technology and a competitive bidding process, we will be able to obtain the necessary capacity for less. Lighting our intercity fiber network may be strategically beneficial to XO because it provides a lower cost basis for future augments enabling faster and more profitable growth.

Our intercity fiber network is a twenty year indefeasible exclusive right to use 18 fiber optic strands pursuant to arrangements with Level 3, substantially all of which are currently unlit. These fibers are part of a fiber network that traverses over 16,000 miles and connects more than 60 cities in the United States and Canada, including most of the major metropolitan markets served by our metro fiber networks. Fiber optic capacity that is not currently connected to transmission equipment is referred to in our industry as unlit.

Along specific segments of our intercity network where the demand for telecommunications capacity justifies the required capital expenditures, we have proceeded with lighting those specific segments. During 2004 we lit intercity fiber in the following segments: San Diego to Phoenix, Chicago to Detroit and Detroit to Cleveland. In prior years we have lit intercity fiber in the flowing segments: Los Angeles to San Diego and Denver to Salt Lake City. Additionally, we previously lit fiber acquired from AboveNet, formerly known as Metromedia Fiber Network, Inc. that runs from New York to Washington, D.C. to provide an additional route to the lit intercity fiber network along that segment and we have also lit fiber in Texas. Based on current pricing and demand projections, we may light another three to nine segment routes in 2005.

Our IP network consists of an OC-192 capacity backbone running through or adjacent to our intercity fiber network. Our IP backbone connects to our intercity fiber network at nine IP backbone nodes, 62 local facilities in 34 markets, and two hosting data centers. Each IP backbone node provides intercity IP transport between each of our metro fiber networks and connectivity to other Internet Service Providers or ISPs, which is commonly referred to as peering. Peering with other ISPs is done in each of our IP backbone facilities except for Denver.

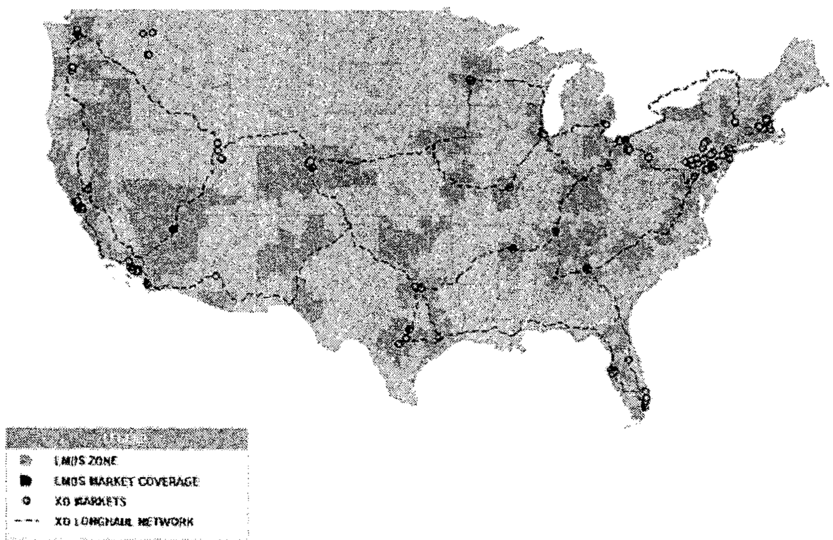
Broadband Wireless

In addition to our fiber and equipment assets, we hold licenses for 1,150 to 1,300 MHz of local multipoint distribution services, or LMDS, spectrum in 59 cities. Our licenses also include:

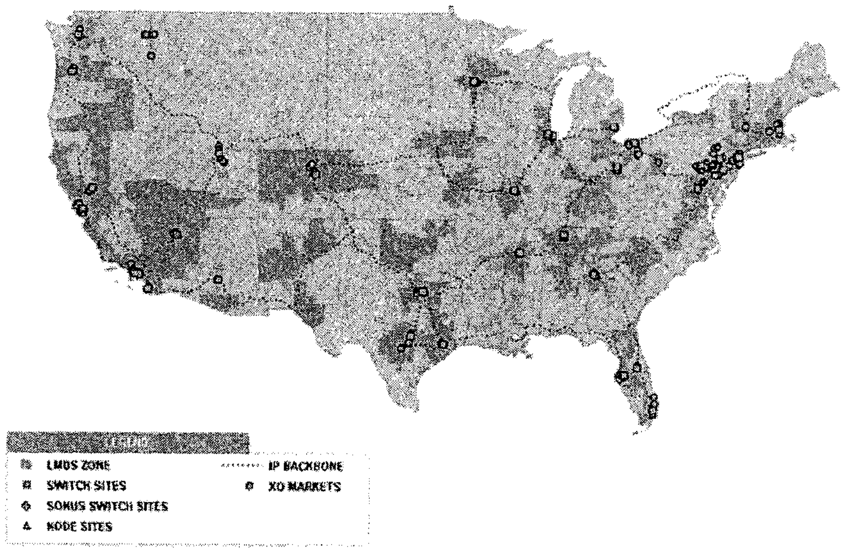
- 150 MHz of LMDS spectrum in 14 other cities;
- 150 MHz of LMDS spectrum in the five boroughs that comprise New York City (300 MHz total); and
- 400 MHz of LMDS spectrum in Denver.

We also hold ten broadband wireless licenses in the 39 GHz (gigahertz) frequency band, of which five provide from 100 to 300 additional MHz in two cities where we hold a 150 MHz LMDS license, plus 100 MHz in Denver and 200 MHz of spectrum in Las Vegas, where we do not hold a LMDS license.

The following diagrams depict the physical components of our nationwide network. There are additional maps located on our web site at www.xo.com. The map below depicts our intercity fiber network and the geographic zones in which we are licensed to deploy fixed wireless services, as well as the local markets in which we are currently able to cost-effectively deploy fixed wireless solutions.



The map below depicts our IP backbone and the facilities related to its operation, such as Sonus IP switches and network IP nodes.



Connecting Customers to Our Networks

We connect our customers directly to our networks through one of three methods. In most cases, we lease ILEC network elements at either cost-based UNE or special access retail rates that connect our facilities directly to our customers' premises, known in our industry as "local loops." Alternatively, we connect customers to our networks by using fiber optic cable and a direct connection to our network. Third, we connect our customers directly to our networks using fixed broadband wireless equipment.

Leasing UNEs. In the majority of cases, we lease facilities from an ILEC to connect a customer to our network, and we attempt to minimize the cost of leasing that capacity by minimizing the distance from our network to a potential customer. Because the cost of leasing those facilities is generally based on the distance of the leased connection, shorter distance connections are less expensive than longer distance connections. One of the most significant advantages of our acquisition of the telecommunications assets of Allegiance was our addition of nearly 833 unique collocations for a combined total of 953 unique collocations. The Allegiance acquisition also added approximately 8,000 metro fiber miles and 2,000 intercity fiber miles to XO for a combined total of 888,000 metro fiber miles and 290,000 intercity fiber miles. This additional local network will allow us to access some of our existing customers and many potential customers more cost effectively than which we were previously able to do so.

Direct Fiber Connection. In cases where the anticipated revenues justify the construction cost, we will install a new fiber optic extension from our network to the customer's premises. Whether it is economical to construct a fiber optic extension depends, among other things, on:

- the existing and potential revenue base located in the building in question;
- the building location relative to our network and our ability to access the communications equipment in that building, and

• local permit requirements, landlord requirements, and construction costs.

Direct Fixed Broadband Wireless Connection. In limited cases where economically and technologically feasible, we may deploy a high-bandwidth fixed wireless connection between an antenna on the roof of the customer's premises and an antenna attached to our metro fiber network. In those cases, we must secure roof and other building access rights, including access to conduits and wiring from the owners of each building or other structure on which we propose to install our equipment, and may need to obtain construction, zoning, franchise or other governmental permits.

Network Technology

Over the past few years, both optical and IP-based networking technologies have undergone rapid innovation. Many of these innovations have the effect of increasing the efficiency of the physical components of our network by increasing the effective capacity of networks for these types of applications. In the future, we expect that IP-based technology will become the preferred technology for voice calls and facsimile transmission as well. We believe that our IP-based service platform will provide us with significant future opportunities, because it enables data, voice and video to be carried less expensively and more efficiently over our end-to-end, facilities-based network. Consequently, we have made and will continue to make significant investments in supplementing our data and voice switching technology with IP equipment.

Voice Switching Technology. There are two commonly used switching technologies currently deployed in most telecommunications networks: circuit switched-based systems and packet switched-based systems. Circuit switch-based systems are currently used on the PSTN and most telecommunications networks. Circuit switch-based systems establish a dedicated channel for each telecommunication signal (such as a telephone call for voice or fax), maintain the channel for the duration of the call, and disconnect the channel at the conclusion of the call.

Packet switch-based telecommunications systems, which format the information to be transmitted into a series of shorter digital messages called "packets," are the preferred means of data transmission. Packet-switched telecommunications technology is the foundation for VoIP and delivery of voice communications via the Internet. In packet switching, each packet consists of a portion of the complete message plus the addressing information to identify the destination and return address. A key feature that distinguishes Internet architecture and packet switching from the PSTN and circuit switching is that on the packet-switched Internet, a single dedicated channel between telecommunication points is not required as it is in circuit switched communications.

Packet switch-based systems offer several advantages over circuit switch-based systems, including the ability to commingle packets from several telecommunications sources, particularly those with bursts of information followed by periods of "silence," the ability to commingle packets provides for superior network utilization, and efficiency, resulting in more information being transmitted through a given telecommunication channel. We currently carry more than 90% of our voice and data traffic in packetized form over our intercity network.

XO was one of the early adopters of softswitch and VoIP technologies. XO's voice switching strategy relies on strategic integration of our circuit technology switches and IP-based Sonus softswitch network. We have designed our network to provide both flexibility and high quality service. XO has 60 Nortel DMS-500 and Lucent 5ESS circuit switches in its network providing a rich array of services, national presence and connectivity to the PSTN. Our Sonus softswitch network, which enables the deployment of VoIP technology, has been in service since 2001. The Sonus network has more than 80 gateways in 33 markets interconnected by a high capacity IP network. The Sonus network fully interoperates with the Nortel and Lucent circuit switches and has connectivity to the national common channel signaling network to access industry databases such as number portability databases. The Sonus network carries several hundred million minutes of usage per month of traffic resulting from toll free, long distance and ISP offload services.

The rapid advance of using packet technology for voice has brought to market several new types of service providers that want to offer voice services using IP transmission but that do not wish to invest in establishing a softswitch network. XO, with its Sonus network and extensive connectivity to the PSTN, is positioned to provide connectivity to these VoIP service providers. XO is currently offering products to allow these service providers to transfer such IP traffic to XO in its IP form, as opposed to the traditional requirement that such traffic be converted to the PSTN traffic protocol.

Packet communication for voice and other technologies allows XO to offer enhanced services and to enable our business customers to efficiently connect to our network for their voice, data, and other private data networking needs. This cost-effective connection to our network would not be possible through traditional circuit switching technology because, in the absence of IP transmission, our customers would be required in many cases to access our network through switching and other facilities owned by third party carriers. This capability allows greater utilization of XO's network assets than a circuit switched solution, with virtually no degradation in service to customers, and allows XO to offer all of those services on a single connection to the customer's premises.

Use of packet-based transport also allows XO to leverage its IP backbone for a variety of other uses. In addition to having voice services supplied across the IP network, XO can provide a variety of private data network connectivity including Frame-Relay and Ethernet to provide XO's customers secure data transport between customer locations. For customer locations that are directly connected to XO's fiber network, XO can utilize technologies such as Ethernet for transport of customer data from the customer premises to our network which further increase XO's network efficiency and allows our customers to use an operationally less complex and inexpensive connection method as compared to older circuit switching technologies. To increase our ability to provide Ethernet connectivity for customers who are not directly connected to our network via fiber, we utilize Ethernet transport over copper and other existing ILEC facilities to provide that customer-preferred interconnection. We believe that packet switching will eventually replace circuit switched technologies and will be the foundation of integrated networks which treat all transmissions, including voice, fax, and video, simply as forms of data transmission.

Fixed Broadband Wireless Technology. We are the licensee of the largest U.S. footprint of fixed wireless spectrum. We deploy fixed broadband wireless connections pursuant to 91 LMDS spectrum licenses issued to us by the FCC exclusively or nonexclusively through which all of our currently deployed wireless applications have been provided, and ten additional 39GHz licenses available to us, but through which we have not yet deployed any wireless applications. We currently deploy LMDS connections in very limited circumstances. The following tables shows (i) the license number, (ii) the metropolitan areas and frequency band for each area covered by the license, (iii) the estimated population for each area, (iv) the amount of spectrum for each area, and (v) the expiration date for each license.

License Number	City	State	Population	A Band	B Band	39 GHz Chanls	License Renewal
WPOL286	New York (PMSA of 5 boroughs & 3 counties)	NY	8,546,846	A3			2/01/2006
WPLM417	Atlanta	GA	3,197,171		B		6/17/2008
WPLM412	Austin	TX	899,361		B		6/17/2008
WPLM416	Baltimore	MD	2,430,563		B		6/17/2008
WPLM430	Birmingham	AL	1,200,336	A			6/17/2008
WPLM413	Boston	MA	4,133,895		B		6/17/2008
WPLM418	Chattanooga	TN	510,860	A			6/17/2008
WPLM405	Chicago	IL	8,182,076		B		6/17/2008
WPLM424	Cincinnati	OH	1,990,451		B		6/17/2008
WPLM422	Cleveland-Akron	OH	2,894,133		B		6/17/2008
WPLM410	Columbia	SC	568,754	A			6/17/2008
WPLM438	Columbus	OH	1,477,891		B		6/17/2008
WPON926	Denver	CO	2,073,952	A1(part)			6/17/2008
WPLM408	Detroit	MI	4,705,164		B		6/17/2008
WPLM398	Hartford	CT	1,123,678		B		6/17/2008
WPLM411	Hickory-Lenoir-Morganton	NC	292,409	A			6/17/2008

License Number	City	State	Population	A Band	B Band	39 GHz Chanls	License Renewal
WPLM431	Huntsville	AL	439,832	A			6/17/2008
WPLM435	Indianapolis	IN	1,321,911		B		6/17/2008
WPLM436	Kansas City	MO	1,839,569		B		6/17/2008
WPLM434	Klamath Falls	OR	74,566		B		6/17/2008
WPLM420	Lakeland-Winterhaven	FL	405,382		B		6/17/2008
WPLM429	Lexington	KY	816,101	A			6/17/2008
WPLM401	Los Angeles*	CA	14,549,810	A			6/17/2008
WPLM428	Louisville	KY	1,352,955	A			6/17/2008
WPLM423	Mansfield	OH	221,514		B		6/17/2008
WPLM433	Medford-Grants Pass	OR	209,038		B		6/17/2008
WPOH970	Milwaukee	WI	1,751,525	A			6/17/2008
WPLM419	Minneapolis-St. Paul	MN	2,840,561	A			6/17/2008
WPOH945	New Haven-Waterbury- Meriden	CT	978,311		B		6/17/2008
WPLM400	New London- Norwich	CT	357,482		B		6/17/2008
WPLM397	New York (whole BTA)	NY	18,050,615		B		6/17/2008
WPLM421	Ocala	FL	194,833		B		6/17/2008
WPLM432	Portland	OR	1,690,930	A			6/17/2008
WPOH956	Providence-Pawtucket, New Bedford- Fall River	RI,MA	1,509,789	A			6/17/2008
WPLM437	Rochester	NY	1,118,963		B		6/17/2008
WPLM407	Sacramento	CA	1,656,581	A			6/17/2008
WPLM402	San Diego	CA	2,498,016		B		6/17/2008
WPLM406	San Francisco- Oakland- San Jose	CA	6,420,984		B		6/17/2008
WPLM404	San Luis Obispo	CA	217,162	A			6/17/2008
WPLM403	Santa Barbara- Santa Maria	CA	369,608	A			6/17/2008
WPLM427	Seattle-Tacoma	WA	2,708,949	A			6/17/2008
WPLM425	St. Louis	MO	2,742,114		B		6/17/2008
WPLM409	Toledo	OH	782,184		B		6/17/2008
WPLM415	Washington	DC	4,118,628		B		6/17/2008
WPOH677	Albuquerque	NM	688,612	A			9/1/2008
WPOH679	El Paso	TX	649,860	A			9/1/2008
WPOH676	Tucson	AZ	666,880	A			9/1/2008
WPOH683	Lawton-Duncan	OK	177,830	A			9/1/2008
WPOH682	Oklahoma City	OK	1,305,472	A			9/1/2008
WPOH684	Omaha	NE	905,991	A			9/1/2008
WPOH676	Tulsa	OK	836,559	A			9/1/2008
WPOH944	Albany-Schenectady	NY	1,028,615	A			10/6/2008
WPOH963	Atlanta	GA	3,197,171	A			10/6/2008
WPOH954	Austin	TX	899,361	A			10/6/2008
WPOH962	Baltimore	MD	2,430,563	A			10/6/2008
WPOH955	Boston	MA	4,133,895	A			10/6/2008
WPOH955	Buffalo-Niagara Falls	NY	1,231,795	A			10/6/2008
WPOH950	Charlotte-Gastonia	NC	1,671,037	A			10/6/2008
WPOH948	Chicago	IL	8,182,076	A			10/6/2008
WPOH953	Dallas	TX	4,329,924	A			10/6/2008
WPOH975	Des Moines	IA	728,830	A			10/6/2008
WPOH949	Detroit	MI	4,705,164	A			10/6/2008
WPOH952	Greenville-Spartanburg	NC	788,212	A			10/6/2008
WPOH943	Hartford	CT	1,123,678	A			10/6/2008
WPOH966	Houston	TX	4,054,253	A			10/6/2008
WPOH974	Indianapolis	IN	1,321,911	A			10/6/2008
WPOH979	Jacksonville	FL	1,114,847	A			10/6/2008
WPOH981	Knoxville	TN	948,055	A			10/6/2008
WPOH947	Los Angeles	CA	14,549,810		B		10/6/2008
WPOH959	Manchester-Nashua- Concord	NH	540,704	A			10/6/2008
WPOH973	Memphis	TN	1,396,390	A			10/6/2008
WPOH967	Miami-Ft. Lauderdale	FL	3,270,606	A			10/6/2008
WPLM426	Milwaukee	WI	1,751,525		B		10/6/2008
WPOH964	Minneapolis- St. Paul	MN	2,840,561		B		10/6/2008
WPOH980	Nashville	TN	1,429,309	A			10/6/2008

License Number	City	State	Population	A Band	B Band	39 GHz Chanls	License Renewal
WPLM399	New Haven-Waterbury- Meriden	CT	978,311	A			10/6/2008
WPOH942	New York (unencumbered by PMSA)	NY	9,503,769	A			10/6/2008
WPOH960	Philadelphia, Wilmington (DE), Trenton (NJ)	PA	5,899,345	A			10/6/2008
WPOH971	Pittsburgh	PA	2,507,839	A			10/6/2008
WPLM414	Providence-Pawtucket, New Bedford- Fall River	RI,MA	1,509,789		B		10/6/2008
WPOH951	Raleigh-Durham	NC	1,089,423	A			10/6/2008
WPOH972	Richmond-Petersburg	VA	1,090,869	A			10/6/2008
WPOH978	Rochester	NY	1,118,963	A			10/6/2008
WPOH976	San Antonio	TX	1,530,954	A			10/6/2008
WPOH958	Springfield-Holyoke	MA	672,970	A			10/6/2008
WPOH969	St. Louis	MO	2,742,114	A			10/6/2008
WPOH946	Syracuse	NY	791,140	A			10/6/2008
WPOH965	Tampa-St. Petersburg- Clearwater	FL	2,249,405	A			10/6/2008
WPOH961	Washington	DC	4,118,628	A			10/6/2008
WPOH968	West Palm Beach- Boca Raton	FL	893,145	A			10/6/2008
WPOH957	Worcester-Fitchburg- Leominster	MA	709,705	A			10/6/2008
WPQT938	Denver-Boulder- Greeley	CO	2,073,952			B	10/18/2010
WPQT942	Las Vegas	NV	857,856			E	10/18/2010
WPQT946	Las Vegas	NV	857,856			G	10/18/2010
WPQT939	San Diego	CA	2,498,016			B	10/18/2010
WPQT944	San Diego	CA	2,498,016			F	10/18/2010
WPQT947	San Diego	CA	2,498,016			N	10/18/2010
WPQT940	San Francisco	CA	6,420,984			D	10/18/2010
WPQT945	San Francisco	CA	6,420,984			F	10/18/2010
WPQT941	Toledo	OH	782,184			E	10/18/2010
WPQT943	Toledo	OH	782,184			F	10/18/2010

Legend	
A	27,500 to 28,350 MHz, 29,100 to 29,250 GHz, 31,075 to 31,225 GHz = 1,150 MHz
A1	27,500 to 28,350 MHz = 850 MHz
A3	31,075 to 31,225 GHz = 150 MHz
B	31,000 to 31,075 MHz, 31.225 to 31,300 MHz = 150 MHz
39 GHz B	38,650 to 38,700 MHz, 39,350 to 39,400 = 100 MHz
39 GHz E	38,800 to 38,850 MHz, 39,500 to 39,550 = 100 MHz
39 GHz G	38,900 to 38,950 MHz, 39,600 to 39,650 = 100 MHz
39 GHz F	38,850 to 38,900 MHz, 39,550 to 39,600 = 100 MHz
39 GHz N	39,250 to 39,300 MHz, 39,950 to 40,000 = 100 MHz
39 GHz D	38,750 to 38,800 MHz, 39,450 to 39,500 = 100 MHz
	The higher the frequency, the higher the attenuation (loss). For the same amount of transmission power, a lower frequency signal will propagate farther.

The spectrum under the licenses we hold can transmit voice, data or video signals from one fixed antenna to one or many others. As the word "local" in the local multipoint distribution service name implies, the radio links using LMDS frequencies are of limited distance, typically five miles or less, due to the degradation of these high-frequency signals over greater distances.

There are additional holders in some of the cities where we hold licenses. There are also competitors who are licensed broadband fixed wireless operators in the 39 GHz spectrum bands. Examples include First Avenue Networks and AT&T Business Services. There are existing users of the 39 GHz spectrum that may require XO as a new user of the spectrum to coordinate its use to avoid interference with an existing user. We do not believe that the coordination process will significantly limit our ability to use the spectrum.

The term of each of the licenses for our broadband wireless spectrum generally is ten years. Although the licenses are renewable for an additional ten year term, renewal is conditioned on our ability to satisfy utilization requirements established by the FCC. The first license expiration is in 2006. We have applied for a two year extension from the FCC, and anticipate that the extension will be approved. We continue to evaluate recent improvements in the price and performance of fixed wireless equipment, and have plans to meet the FCC's "substantial service" test before the licenses are due for renewal proceedings. If we do not meet the FCC's substantial service test at the end of the license expiration date, we may request an extension of time or waiver of license forfeiture from the FCC.

Employees

As of December 31, 2004 we employed approximately 5,000 people, including full-time and part-time employees. Overall, we consider our employee relations to be good. None of our employees is covered by a collective bargaining agreement.

Sales Overview

Our sales organization includes both direct and indirect sales representatives.

Direct Sales. Our direct sales and sales support organization consisted of more than 1,200 employees at December 31, 2004. Our direct sales force includes two sales organizations, one that addresses the needs of commercial retail customers and one that services wholesale carrier accounts. Our commercial sales organization focuses on our SMB customers, developing multi-market accounts and national accounts. Our carrier sales organization focuses solely on servicing telecommunications providers who, in combination with other capabilities, provide telecommunications services under their own brand. Our carrier customers benefit from our national network, our data service capabilities, our broad range of services and our cost effective solution design. In addition, as a result of the recent limitations on the availability of cost-based UNE rates for local transport imposed by the FCC TRRO, as discussed in greater detail below, we believe that our extensive local network may provide additional opportunities for carrier accounts.

We have structured our sales efforts to develop a direct and personal relationship with our customers. We have integrated the Allegiance and XO sales forces with an effort to retain the most productive representatives. We have restructured our compensation formula for our direct sales force in 2005 to reward our salespeople for services that we install and provision to a customer and for ongoing services purchased by that customer over time versus at the point of sale. We train our sales force regularly and will continue to emphasize training in 2005. We believe that this compensation and benefit structure will further our corporate strategy of maximizing profitable revenue growth and promote long term, service-focused relationships with our customers.

Indirect Sales Representatives. We have complemented our direct sales force with over 5,000 third party sales agents to distribute the products and services available to our customers. We currently have distribution arrangements with a number of national, regional and local agents and agency firms, whose representatives market a broad range of XO services. The deployment of indirect sales agents also furthers our strategy of increasing our profitable revenue, as we do not incur costs for indirect sales agents unless and until a sale is made and installed.

Network Services

Our network services organization consists of more than 1,700 employees whose main objective is to deliver superior service and to enhance the customers' experience. Network service employees are located in all of our markets. Their main objectives include the design, deployment, and maintenance of our network assets. In addition, they are responsible for installing customer premise equipment and activating new customers as well as maintaining and, when necessary, repairing any service outages our customers might experience. To be proactive in repairing any network outages and to maintain the highest network quality, we have a 24x7 network operations center with a full network surveillance system.

Customer Care

Once a customer's services have been installed, our customer care operations support customer retention and satisfaction. Our goal is to provide customers with a customer care group that has the ability and resources to respond to and resolve customer questions and issues as they arise. We conduct much of our customer care operations from two call centers. We also provide locally-based care for many large customers. We have integrated the XO and Allegiance customer care organizations, and support the needs of the combined businesses with 600 customer care representatives.

Competition

We compete with a large number of telecommunications services providers in each of our target customer markets.

Incumbent Carriers. In each of our 70 markets, the ILEC generally maintains a dominant market position in the delivery of local exchange services. We compete with ILECs such as Verizon, SBC, Qwest and BellSouth on the basis of our ability to provide nationwide service, our commitment to customer service, and, where our cost structure permits, on the basis of price. If, however, SBC and Verizon or Qwest complete their acquisitions of AT&T and MCI, respectively, SBC and Verizon or Qwest will also be able to offer services nationally. While we believe that we have competitive advantages over the ILECs, each of the ILECs is significantly larger than we are in annual revenues, total assets, and financial resources, and have increased their marketing to our target market of SMBs. In addition, the recent TRRO included several rulings favorable to incumbent carriers, including the elimination in specific central offices of the requirement that the incumbent carriers lease last mile connections to competitive carriers like us at cost-based, UNE rates.

Competitive Local Exchange Carriers. In addition to competing with the ILECs, we also compete with many CLECs, most of which are regionally focused. In general, CLECs often maintain a market or competitive focus that enables them to be successful with specific products or in specific geographic or customer segments. Consequently, in each of our markets, we compete with CLECs who may have different competitive focuses. While we believe that our national reach and breadth of products makes us competitive with nearly any telecommunications carrier, we have to address a wide range of competitive conditions in each of our markets.

Long Distance Companies. Many of the long distance telecommunications services providers, such as AT&T, MCI, and Sprint, also operate national networks. While long distance carriers such as AT&T and MCI have experienced declining revenues in recent years, these long distance carriers remain significantly larger than we are in annual revenues, total assets, and financial resources. In addition, several of these companies have continued to achieve significant competitive success with business customers.

Data and Internet Services Companies. There are a number of large Internet service providers with which we compete in providing various Internet access and data products. Such competitors include Level 3, Global Crossing, and Covad Communications.

VoIP Carriers. Several companies have initiated VoIP services in recent years, including Vonage, Covad, Qwest, and AT&T, that provide voice telecommunications services exclusively by means of IP.

Cable-Based Service Providers. Several companies historically focused on the delivery of cable television services have expanded their service offerings to include broadband connections and, in some cases, local voice services. While several such competitors, such as Comcast, Cox Communications, and Time Warner have focused on the residential market for voice communications services, many of these competitors are significantly larger than we are in annual revenues, total assets, and financial resources. While we believe that we enjoy competitive advantages over such companies because of our industry experience in providing telecommunications services, many large cable providers may build a substantial residential customer base and market to our core SMB market in the future.

Company History

Our principal executive and administrative offices are located at 11111 Sunset Hills Road, Reston, Virginia 20190 and our telephone number is (703) 547-2000. Our Internet address is www.xo.com, where, under "About XO-Investor Center", you can find copies of our annual report on Form 10-K as of and for the year ended December 31, 2004, and our quarterly reports on Form 10-Q and current reports on Form 8-K and amendments thereto, all of which we make available as soon as reasonably practicable after the report is filed with the Securities and Exchange Commission, or the Commission.

The initial predecessor entity of XO was formed as a Washington limited partnership in 1994. In 1995, that entity merged into a Washington limited liability company that became known as "NEXTLINK Communications, L.L.C." In January 1997, NEXTLINK Communications, L.L.C. merged into NEXTLINK Communications, Inc., a Washington corporation, which in June 1998 reincorporated in Delaware under the same name. On June 16, 2000, in connection with the acquisition of Concentric Network Corporation, NEXTLINK Communications, Inc. merged with and into a new corporation and that corporation, as the surviving corporation in the merger, changed its name to NEXTLINK Communications, Inc. On September 25, 2000, NEXTLINK Communications, Inc. began doing business as "XO Communications" and, on October 25, 2000, changed its name to XO Communications, Inc. We conduct our business primarily through the more than 20 subsidiaries that XO owns and manages.

In December 2001, XO voluntarily delisted its pre-petition class A common stock from the Nasdaq National Market, which was traded under the symbol "XOXO", and, on December 17, 2001, began trading on the Over-the-Counter Bulletin Board, or OTCBB. On June 17, 2002, we filed for protection under the Bankruptcy Code. On November 15, 2002, the Bankruptcy Court confirmed our plan of reorganization, and, on January 16, 2003, we consummated the plan of reorganization and emerged from our Chapter 11 reorganization proceedings with a significantly restructured balance sheet.

On June 23, 2004, we acquired the telecommunication services assets of Allegiance, for approximately $325.2 million in cash and approximately 45.38 million shares of our common stock.

During the fourth quarter of 2004, we completed a legal entity reorganization of our operating subsidiaries. We consolidated approximately 75 of our operating subsidiaries with and into a new, nationally-licensed operating company called XO Communications Services, Inc., or XOCS, a directly, wholly-owned subsidiary of XO Communications, Inc. We anticipate that nearly all of our consolidated revenues from the sale of regulated telecommunications services will be earned either by XO or XOCS.

Regulatory Overview

Overview

We are subject to regulation by federal, state and local government agencies. Historically, the FCC had jurisdiction over interstate long distance services and international services, while state regulatory commissions had jurisdiction over local and intrastate long distance services. The Telecommunications Act of 1996, or the "Telecom Act" fundamentally changed the way telecommunications is regulated in this country. The FCC was given a major role in writing and enforcing the rules under which new competitors could compete in the local marketplace. Those rules, coupled with additional rules and decisions promulgated by the various state regulatory commissions, form the core of the regulatory framework under which we operate in providing our services.

With a few limited exceptions, the FCC continues to retain exclusive jurisdiction over our provision of interstate and international long distance service, and the state regulatory commissions regulate our provision of intrastate local and long distance service. Additionally, municipalities and other local government agencies may regulate limited aspects of our business, such as use of government-owned rights-of-way, and may require permits such as zoning approvals and building permits.

The Telecom Act and the related rules governing competition issued by the FCC, as well as pro-competitive policies already developed by state regulatory commissions, have enabled new entrants like us to capture a portion of the ILECs' market share of local services. However, there have been numerous attempts to limit the pro-competitive policies in the local exchange services market through a combination of proposed federal legislation, adoption of new rules by the FCC, and ILEC challenges to existing and proposed regulations. To date, the ILECs have succeeded in eliminating some of the market-opening regulations adopted by the FCC and the states through numerous court challenges. In particular, the ILECs appealed, and won partial reversals of, a series of FCC orders defining the ILEC facilities — known as unbundled network elements or "UNEs" — that ILECs must lease to competitors at cost-based rates. We expect the ILEC's efforts to scale back the benefits of the Telecom Act and local service competition to continue. However, while the FCC has eliminated certain UNEs, the basic framework of local competition, including the UNE regime itself, has remained intact. The successful implementation of our business plan is predicated on the assumption that the basic competitive framework and pro-competitive safeguards will remain in place.

The passage of the Telecom Act largely preceded the explosive growth of the Internet and IP communications. Congress is currently considering whether to further amend the Telecom Act to, among other things, directly address IP communications. It is possible that any such amendment to the Telecom Act could eliminate or materially alter the market-opening regulatory framework of the Telecom Act in general, and the UNE regime in particular. Such a result could adversely affect XO's business. It is not possible to predict if, when, or how the Telecom Act will be amended.

Federal Regulation

The FCC exercises jurisdiction over our telecommunications facilities and services. We have authority from the FCC for the installation, acquisition and operation of our wireline network facilities to provide facilities-based domestic interstate and international services. In addition, we have obtained FCC authorizations for the operation of our LMDS and 39 GHz broadband wireless facilities. Because XO is not dominant in any of its markets, unlike ILECs, we are not currently subject to price cap or rate of return regulation. Thus, our pricing policies for interstate and international end user services are only subject to the federal guidelines that charges for such services be just, reasonable, and non-discriminatory. The FCC allows us to file interstate tariffs for our interstate access services (rates charged by us to other carriers for access to our network). As for domestic and international long distance services, the FCC requires us to make the terms, conditions and rates of the detariffed services available to the public on XO's web page, and such terms, conditions, and rates are located at http://www.xo.com/legal/.

Implementation of the Telecom Act

The Telecom Act's Local Competition Framework

One of the key goals of the Telecom Act is to encourage competition in the provision of local telephone service. To do this, the Telecom Act provides three means by which CLECs such as XO can enter the local telephone service market. The three modes of entry are as follows:

- *Access to UNEs.* ILECs are required to lease to CLECs various elements in their network that are used individually or in combination with each other to provide local telephone service. As discussed in more detail below, the FCC determines which facilities must be made available by the ILECs as UNEs. The ILECs must make UNEs available at rates that are based on their forward-looking economic costs, a pricing regime known as "TELRIC," short for Total Element Long Run Incremental Cost. For XO, the most critical UNEs are local loops and transport, which enable us to connect our customers to our network.
- *Construction of New Facilities.* CLECs may also enter the local service market by building entirely new facilities. The ILECs are required to allow CLECS to interconnect their facilities with the ILECs' facilities in order to reach all customers.
- *Resale.* ILECs are required to permit CLECs to purchase their services for resale to the public at a wholesale rate that is less than the rate charged by the ILECs to their retail customers.

To facilitate competitors' entry into local telephone markets using one or more of these three methods, the Telecom Act imposes on the ILECs the obligation to open their networks and markets to competition. When requested by competitors, ILECs are required to negotiate, in good faith, agreements that set forth terms governing the interconnection of their network, access to UNEs, and resale. XO has negotiated interconnection agreements with the ILECs in each of the markets in which it operates. Many of these interconnection agreements are being renegotiated now.

The following is a summary of the interconnection and other rights granted by the Telecom Act that are important for effective local service competition and our belief as to the effect of those requirements, if properly implemented:

- interconnection with the networks of incumbents and other carriers, which permits our customers to exchange traffic with customers connected to other networks;
- requirements that the ILECs make available access to their facilities for our local loops and transport needs, thereby enabling us to serve customers not directly connected to our networks;
- compensation obligations, which mandate reciprocal payment arrangements for local traffic exchange between us and both incumbent and other competitive carriers and compensation for terminating local traffic originating on other carriers' networks;
- requirements concerning local number portability, which allows customers to change local carriers without changing telephone numbers, thereby removing a significant barrier for a potential customer to switch to our local voice services;
- access to assignment of telephone numbers, which enables us to provide telephone numbers to new customers on the same basis as incumbent carriers; and
- collocation rights allowing us to place telecommunications equipment in ILEC central offices, which enables us to have direct access to local loops and other network elements.

Although the rights established in the Telecom Act are a necessary prerequisite to the introduction of full local competition, they must be properly implemented and enforced to permit competitive telephone companies like XO to compete effectively with the incumbent carriers. Discussed below are several FCC and court proceedings relating to the application of certain FCC rules and policies that are significant to and directly impact our operations and costs as well as the nature and scope of industry competition.

Unbundling of Incumbent Network Elements

In a series of orders and related court challenges that date back to 1996, the FCC has promulgated rules implementing the market-opening provisions of the Telecom Act, including the requirement that the ILECs lease UNEs to competitors at cost-based rates. At the core of the series of FCC orders is the FCC's evolving effort to define which ILEC network facilities must be made available as UNEs. Initially, the FCC defined a broad list of UNEs, consisting of most of the elements of the ILECs' networks. Under pressure from the ILECs, the FCC has subsequently reduced the list, while preserving access to those network elements critical to the operation of XO's business.

The current list of UNEs was promulgated by the FCC in two orders. The first is the Triennial Review Order, or "TRO", which was released on August 21, 2003. Several carriers and other entities appealed the FCC's TRO decision. On March 2, 2004, the U.S. Court of Appeals for the D.C. Circuit issued its opinion in United States Telecom Association v. FCC, No. 00-1012 ("USTA II Decision"). In the USTA II Decision, the court reversed and overturned many of the conclusions of the TRO. In the aftermath of the USTA II Decision, the FCC released the second of its two currently controlling orders, the TRO Remand Order or "TRRO", on February 4, 2005. It is expected that various parties will appeal the TRRO. It is not possible to predict the outcome of those appeals. It is possible that portions of the order could be overturned and that the FCC will issue new rules in their place that further restrict access to UNEs.

As of March 11, 2005, the effective date of the TRRO, the ILECs are obligated to provide as UNEs the following network facilities used by XO to serve its customers:

UNE Loops

DS0 loops. A DS0 loop is a single, voice-grade channel. Typically, individual business lines are DS0 loops. The ILECs must make DS0 loops available at UNE rates on an unlimited basis.

DS1 loops. A DS1 loop is a digital loop with a total speed of 1.544 megabytes per second, which is the equivalent of 24 DS0s. Multiple voice lines and Internet access can be provided to a customer over a single DS1 loop. We serve most of our customers with DS1 loops. The ILECs must provide DS1 loops at UNE rates at the majority of their central offices. Competitors, however, are limited to no more than 10 DS1 loops to any particular building.

DS3 loops. A DS3 loop is a digital loop with a total speed of 44.736 megabytes per second. In some cases, XO serves its large business customers with DS3 loops. ILECs must provide DS3 loops at UNE rates at the majority of their central offices. Competitors, however, are limited to no more than one DS3 loop to any particular building.

As of the TRRO, ILECs are not required to provide optical capacity loops or dark fiber loops as UNEs. Optical capacity loops, referred to as OCn loops, are very high-capacity digital loops ranging in capacity from OC3 loops, which are the equivalent of three DS3s to OC192. This will not impact our costs.

The ILECs are also not required to provide certain mass market broadband loop facilities and functionality as UNEs. Under the TRO, the ILECs are not required to make newly-deployed fiber-to-the-home or FTTH loops available as UNEs and are only required to provide the equivalent of DS0 capacity on any FTTH loop built over an existing copper loop. These recent FCC orders should only limit availability for those specific network elements, which are not material to us. It is possible, however, that the ILECs will seek additional broadband regulatory relief in future proceedings.

UNE Transport

DS1 transport. Whether transport is available as a UNE is determined on a route-by-route basis. ILECs must make transport at UNE rates available at DS1 capacity levels between any two ILEC central offices unless both central offices either (1) serve more than 38,000 business lines or (2) have four or more fiber-based collocators. On routes where DS1 transport must be made available, each individual competitor is limited to no more than 10 DS1 transport circuits per route.

DS3 transport. Access to DS3 capacity-level transport is more limited than access to DS1 transport. ILECs must make transport at UNE rates available at DS3 capacity levels between any two ILEC central offices unless both central offices either (1) serve more than 24,000 business lines or (2) have three or more fiber-based collocators. On routes where DS3 transport must be made available, each individual competitor is limited to no more than 12 DS1 transport circuits per route.

Dark fiber transport. Dark fiber transport is available under the same conditions as DS3 transport.

ILECs are not required to provide access to transport at greater-than DS3 capacity levels. ILECs are also not required to provide transport at any capacity level to connect an ILEC central office with a competitor's facilities.

Transitional availability where elements are no longer available as UNEs

For DS1, DS3, and dark fiber loops and transport that do not meet the criteria for availability set forth above, the FCC established a transitional period during which the ILECs must continue to make the elements available at UNE rates to serve existing customers. For DS1 and DS3 loops and transport, the ILECs must make the elements available at 115% of the TELRIC rate for one year beginning on

March 11, 2005. For dark fiber loops and transport, the ILECs must make the elements available at 115% of the TELRIC rate for 18 months beginning on March 11, 2005.

Although these rules adopted by the FCC in the TRRO became effective on March 11, 2005, many of the requirements imposed by the FCC in the TRO and TRRO were not self-executing. Accordingly, the FCC made clear that carriers must follow the change of law procedures in their applicable interconnection agreements with ILECs to implement any TRO requirements that are not self-executing and that carriers must follow the procedures set forth in section 252(b) of the Telecom Act to modify interconnection agreements that are silent as to implementation of changes in law. We have been in negotiations with ILECs to amend our interconnection agreements to implement relevant TRO requirements and, to date, have executed amendments in several states.

Additional Federal Regulations

The following discussion summarizes some additional specific areas of federal regulation that directly affect our business.

VoIP. Like a growing number of carriers, we utilize IP technology for the transmission of a portion of our network traffic. The regulatory status and treatment of IP-enabled services is unresolved. In particular, there is uncertainty as to the imposition of access charges, Universal Service fund contributions, and other taxes, fees, and surcharges on VoIP services. In a recent order, the FCC held that Vonage's VoIP services and similar offerings by other providers are subject to the FCC's interstate jurisdiction, preempting state efforts to regulate VoIP providers as intrastate telecommunications providers. Four separate state commissions have appealed this ruling and the case is currently pending. The FCC, however, left open the question of whether VoIP providers provide "telecommunications" — i.e., basic transmission services — or enhanced "information services." Under the Communications Act, those are mutually exclusive categories. Generally, telecommunications carriers, including traditional local and long distance telecommunications companies are regulated under the Communications Act; information service providers are generally unregulated. The FCC has initiated a rulemaking proceeding to address the classification of VoIP and other IP-enabled service offerings. It is not possible to predict the outcome of that proceeding or its effect on XO's operations. In conjunction with the rulemaking proceeding, the FCC is considering a petition filed on February 5, 2004 by SBC Communications requesting that the FCC forbear from applying common carrier regulation to IP-based networks. Under the Communications Act, the FCC must act on forbearance petitions within one year, or the petition is deemed granted, subject to a single, 90-day extension available to the FCC at its discretion. On December 10, 2004, the FCC exercised its right to extend the deadline for action until May 5, 2005.

AT&T Declaratory Ruling Re: VoIP. On April 21, 2004, the FCC released an order denying AT&T's request that the FCC find that VoIP services are exempt from switched access charges, the AT&T Order. The FCC held that an interexchange service that uses ordinary customer premises equipment that originates and terminates on the PSTN, that provides no enhanced functionality, and that undergoes no net protocol conversion, is a telecommunications service and subject to switched access charges. The order apparently places interexchange services similar to those VoIP services offered by AT&T in the same regulatory category as traditional telecommunications services and, therefore, potentially subjects such VoIP services to access charges and other regulatory obligations including Universal Service fees. Although the FCC did not rule on the applicability of access charges for services provided prior to April 21, 2004, the ILECs may attempt to assert claims against other telecommunications companies including us for the retroactive payment of access charges. On April 22, 2004, SBC Communications filed a collections lawsuit against AT&T and other carriers seeking retroactive payment of unpaid access charges. On February 4, 2005, SBC amended an existing collection case it had filed against Global Crossing and filed a complaint against XO.

Level 3 Forbearance Petition. On December 23, 2003, Level 3 filed a petition requesting the FCC not to apply interstate or intrastate access charges on IP traffic that originates or terminates on the PSTN. If the FCC grants Level 3's petition, we would expect that there would be reductions in our network costs associated with the termination of certain IP-to-PSTN and PSTN-to-IP traffic. If, on the other hand, the FCC rules against Level 3 and adopts rules that require interstate access charges to be paid for the termination of IP-to-PSTN traffic, our network costs will increase. The FCC must rule on Level(3)'s pending petition for forbearance by March 22, 2005 or the petition will be granted.

ILEC Provision of Broadband Telecommunications Services and Information Services. Currently, the ILECs, as dominant carriers, are subject to a relatively high degree of regulation with respect to their broadband serving offerings. The FCC, however, has initiated a rulemaking proceeding in which it is considering deregulating, or applying a lower degree of regulation to, ILEC broadband offerings. If the ILECs are largely freed from dominant carrier regulation, they will have much greater pricing flexibility and will pose a greater competitive threat to XO. In a second, related rulemaking, the FCC is considering whether to eliminate certain requirements it imposes on the ILECs with respect to their broadband Internet access services. Currently, where the ILECs offer Internet access or other information services over broadband facilities, they must (1) purchase the underlying broadband transmission facilities from themselves at tariffed rates and (2) make the underlying facilities available to competitors on a non-discriminatory basis. If the FCC were to eliminate these requirements, it could result in an increase to our network costs. To date, these deregulatory trends have been directed towards facilities used primarily by residential customers, and not by business customers.

Intercarrier Compensation Reform. Currently, telecommunications carriers are required to pay other carriers for interstate access charges and local reciprocal compensation charges. These two forms of intercarrier compensation have been under review by the FCC since 2001. The FCC continues to consider a broad order reforming the intercarrier compensation system and issued a Notice of Proposed Rulemaking on February 10, 2005 to seek further comment on intercarrier compensation reform. Although we are unable to predict the outcome of the FCC's rulemaking procedures, inasmuch as access charges and reciprocal compensation payments make up our largest network expense item, the FCC's action could have a material, adverse affect on our operations and cost of doing business.

Cost-based TELRIC Pricing. On September 10, 2003, the FCC initiated a new proceeding to consider significantly revamping the current TELRIC methodology used for the pricing of UNEs. If the FCC reverses the methodology used for determining UNE rates to allow for rate increases, this could substantially raise XO's costs for leasing UNEs in the future. A decision is expected sometime in 2005. Several state commissions have also initiated proceedings to review the rates that the ILECs charge for UNEs. An adverse ruling in these proceedings would allow the ILECs to increase UNE rates in the applicable state and this could substantially raise our costs for leasing UNEs in the future.

State and Local Regulation

California PUC Proceeding. On September 23, 2004, the California Public Utilities Commission, the CA Commission, issued a decision that requires SBC to adjust monthly recurring rates for certain types of services offered to CLECs by SBC. As a result of this decision, we believe that we are owed a retroactive credit. The billing adjustments and true-up payments required by the decision have been stayed until the CA Commission can: (a) consider mitigations to lessen the negative effect of such true-up payments; and (b) consider issues raised by the Ninth Circuit Court of Appeal regarding the shared and common cost mark-up element. Since the decision, the CA Commission has issued three separate alternate draft decisions which propose different true-up payment schemes and different shared and common cost mark-up factors 10%, 15%, and 21%, respectively. The date that the CA Commission will vote on the draft decisions is unknown at this time, but the next possible date that this issue could be considered by the CA Commission is March 17, 2005. Therefore, we currently are unable to determine the amount or the timing of the expected credit.

In general, state regulatory commissions have regulatory jurisdiction over us when our facilities and services are used to provide local and other intrastate services. Under the Telecom Act, state commissions continue to set the requirements for providers of local and intrastate services, including quality of services criteria. State regulatory commissions also can regulate the rates charged by CLECs for intrastate and local services and can set prices for interconnection by new telecommunications service providers with the ILEC networks, in accordance with guidelines set by the FCC. In addition, state regulatory commissions in many instances have authority under state law to adopt additional regulations governing local competition and consumer protection, so long as the state's actions are not inconsistent with federal law or regulation.

Most state regulatory commissions require companies that wish to provide intrastate common carrier services to register or be certified to provide these services. These certifications generally require a showing that the carrier has adequate financial, managerial and technical resources to offer the proposed services in a manner consistent with the public interest. We are certified in all of the states in which we conduct business. In most states, we are also required to file tariffs setting forth the terms, conditions and prices for services that are classified as intrastate, and to update or amend our tariffs as rates change or new products are added. We may also be subject to various reporting and record-keeping requirements.

Where we choose to deploy our own transmission facilities, we may be required, in some cities, to obtain street opening and construction permits, permission to use rights-of-way, zoning variances and other approvals from municipal authorities. We also may be required to obtain a franchise to place facilities in public rights of way. In some areas, we may be required to pay license or franchise fees for these approvals. We cannot assure you that fees will remain at current levels, or that our competitors will face the same expenses, although the Telecom Act requires that any fees charged by municipalities be reasonable and non-discriminatory among telecommunications carriers.

Risk Factors

Risks Related to Liquidity, Financial Resources, and Capitalization

The covenants in our Credit Agreement restrict our financial and operational flexibility, which could have an adverse affect on our results of operations.

Our Credit Agreement contains covenants that restrict, among other things, the amount of our capital expenditures, our ability to borrow money, grant additional liens on our assets, make particular types of investments or other restricted payments, sell assets or merge or consolidate. A company controlled by Mr. Carl Icahn holds more than 90% of the principal amount of the loans outstanding under the Credit Agreement. Because amendments to or waivers of covenants under the Credit Agreement generally require the approval or consent of holders of only a majority of the outstanding principal amount under the Credit Agreement, decisions whether to amend or waive compliance with such covenants by the holders of loans under the Credit Agreement can be made by Mr. Icahn, whether or not the other holders agree.

Our Credit Facility includes a financial covenant requiring us to maintain minimum earnings before interest, taxes, depreciation, and amortization, or EBITDA, for the twelve-month period ending each fiscal quarter. We did not meet this covenant in 2004 and based on current financial results and our current business plan, we do not expect to comply with this covenant in 2005. We have obtained a waiver through December 31, 2005, but we can not be certain that we will be able to obtain any further waivers of this, or any other, covenant in our Credit Facility. If we are not able to (i) amend this Credit Facility covenant to remove the minimum EBITDA requirements or decrease the requirement to a level we believe we can achieve, (ii) obtain an extension on the waiver to at least March 31, 2006, or (iii) repay the Credit Facility with a new debt or equity offering so that we are in compliance, under the current accounting guidelines we will be required to reclassify the $366.2 million amount outstanding from long term to short term as of March 31, 2005. While the existing waivers prevent the lenders under the Credit Facility from accelerating repayment of the outstanding indebtedness under the Credit Facility until March 31, 2006, this reclassification would cause a significant deterioration to our disclosed working capital and financial position. The security for the Credit Agreement consists of substantially all of the assets of XO and our subsidiaries. A default under the Credit Agreement could adversely affect our rights under other commercial agreements.

The Credit Agreement and the existence of the loans under the Credit Agreement also could affect our financial and operational flexibility, as follows:

- they may impair our ability to obtain additional financing in the future;
- they may limit our flexibility in planning for or reacting to changes in market conditions; and
- they may cause us to be more vulnerable in the event of a downturn in our business.

We may not prevail in our $50 million claim against the Allegiance Telecom Liquidating Trust, and we may not be successful in defending ourselves from the Allegiance Telecom Liquidating Trust's $100 million counterclaim against us.

In August 2004, XO filed an administrative claim against the Allegiance Telecom Liquidating Trust, or ATLT, the successor to the assets and liabilities of Allegiance Telecom, Inc. that we did not acquire. We have claimed that we are entitled to approximately $50 million in damages related to a variety of actions taken by Allegiance and the ATLT. The ATLT filed a counterclaim against us in November 2004 seeking damages of approximately $100 million. We are vigorously pursuing our claims against the ATLT, and we are disputing the ATLT counterclaim as being frivolous and without merit. There can be no assurance, however, that we will be successful in recovering the damages to which we believe we are entitled, or that we will successfully defend ourselves against the ATLT counterclaim, in which case our financial condition and results of operations could be materially and adversely affected.

We incurred a net loss in 2004 and, in the near term, may not generate funds from operations sufficient to meet all of our cash requirements.

For each period since inception, we have incurred net losses. For 2004, we posted a net loss attributable to common stockholders of approximately $410.5 million. In the near term, we expect to use cash to fund our ongoing capital expenditure requirements.

We may not realize the network synergies that we estimate in connection with the acquisition of the Allegiance assets.

While we have been successful in realizing many of the network synergies that we estimated were achievable in connection with the acquisition of the Allegiance assets, and we are confident that we will achieve additional synergies, it is possible that our estimates could prove to be incorrect. For example, we may discover during the process of further integrating the Allegiance assets into our network and business infrastructures that some of the acquired assets require greater maintenance or earlier replacement than originally anticipated. In addition, unanticipated growth in our business as a result of the acquisition of the Allegiance assets may require that some facilities or support functions that we currently anticipate will be combined or reduced may be necessary to retain for us to maintain our operations. The synergies that we anticipate to realize are also dependent on our ability to combine the Allegiance assets with our own network infrastructure in a manner that permits us to realize those synergies. If we have not estimated the potential synergies correctly, or if we are not able to integrate the Allegiance assets into our network infrastructure effectively, we may not realize any further network synergies in connection with the acquisition of the Allegiance assets, or such synergies may take longer to realize.

We are also retaining investment bankers and consultants who will develop and make recommendations to us regarding our strategic alternatives.

Risks Related to Our Operations

The failure of our operations support systems, including the systems for sales tracking, order entry and provisioning, and billing, to perform as we expect could impair our ability to retain customers and obtain

new customers, or provision their services, or result in increased capital expenditures, which would adversely affect our revenues or capital resources.

Our operations support systems are an important factor in our operations. Critical information systems used in daily operations perform sales and order entry, provisioning, billing and accounts receivable functions, and cost of service verification and payment functions, particularly with respect to facilities leased from ILECs. Although we have integrated some systems with respect to the products and customers we acquired from Allegiance Telecom, Inc. we do maintain separate systems for XO and Allegiance in several key areas, such as provisioning. If any of these systems fail or do not perform as expected, or if we fail to coordinate our remaining separately-existing Allegiance and XO systems, such failures would impact our ability to process orders and provision sales, and to bill for services efficiently and accurately, which could, in turn, cause us to suffer customer dissatisfaction, loss of business or the inability to add new customers or additional services to existing customers in a timely basis, any of which would adversely affect our revenues. In addition, system failure or performance issues could impact our ability to effectively audit and dispute invoicing and provisioning data provided by service providers from whom we lease facilities.

Our Disaster Recovery framework to control and address systems risks is not fully redundant, and we may incur the costs, delays and customer complaints associated with system failures. In addition, our ability to efficiently and accurately provision new orders for services on a timely basis is necessary for us to begin to generate revenue related to those services. We have experienced, and may continue to experience, delays and related problems in processing service orders, provisioning sales and billing in connection with the transition to these new systems. If the delays or related problems continue, or if any unforeseen problems emerge in connection with our migration to the new provisioning software and systems, delays and errors may occur in the provisioning process, which could significantly increase the time until an order for new service can begin to generate revenue, which could have a material adverse effect on our operations.

Our rights to the use of the unlit capacity that make up our network may be affected by the financial health of our fiber providers.

We possess the right to use the unlit capacity that is included in our network, particularly in our intercity network, through long-term leases or indefeasible right of use agreements. A bankruptcy or financial collapse of one of these fiber providers could result in a loss of our rights under such leases and agreements with the provider, which in turn could have a negative impact on the integrity of our network, our ability to expand the capacity of our network as our business grows, and ultimately on our results of operations. For example, we lease or have indefeasible rights of use on networks owned and maintained by Level 3. If Level 3 were to encounter severe financial difficulties, we may not be able to maintain or protect our rights in important components of our intercity network. In such an event, there can be no assurance that we will be able to lease comparable strands of unlit capacity if we are not able to retain our rights to use the existing unlit capacity we have obtained from Level 3, nor that we will be able to lease such strands from another provider at competitive or economical rates.

We may not be able to continue to connect our network to the ILEC's network or maintain Internet peering arrangements on favorable terms, which would impair our growth and performance.

We are required to be a party to interconnection agreements with the ILECs in order to connect our customers to the PSTN. If we are unable to renegotiate or maintain interconnection agreements in all of our markets on favorable terms, it could adversely affect our ability to provide services in the affected markets.

Peering agreements with ISPs allow us to access the Internet and exchange traffic with these providers. Depending on the relative size of the providers involved, these exchanges may be made without settlement charge. Recently, many ISPs that previously offered peering have reduced or eliminated peering relationships or are establishing new, more restrictive criteria for peering and an increasing number of these ISPs are seeking to impose charges for transit. Increases in costs associated with Internet and exchange transit could have an adverse effect on our margins for our services that require Internet access. We may not be able to renegotiate or maintain peering arrangements on favorable terms, which would impair our growth and performance.

We may not be able to successfully extend the termination date of our LMDS licenses for New York City and the surrounding vicinity.

Our licenses to use the wireless point-to-point LMDS spectrum for the geographic region that includes New York City are currently scheduled to expire in 2006. Although we have filed applications to extend the deadlines for the expiration of those licenses, there can be no assurance that we will be successful in extending the expiration date of our LMDS licenses in New York City beyond 2006. If we are not successful in extending the expiration date of those licenses, the value would be impaired, and we would adjust our asset balance. In addition, we would not be able to develop our wireless, point-to-point solutions in that market, which could either require us to expend resources to obtain alternative spectrum or curtail our opportunity for developing wireless, point-to-point last mile connectivity in that market.

We depend on a limited number of third party service providers for the performance of selected business operations, and if any such third party service providers were to experience significant interruptions in their business operations, or were to otherwise cease to provide such services, our operations could be materially and adversely affected.

We depend on a limited number of third party service providers for the performance of several our business operations, including payroll and billing services. If any of these third party providers were to experience significant interruptions in their business operations, terminate their agreements with us, or fail to perform the services required under the terms of our contracts with them, our own processing could be materially and adversely affected for a period of time that we can not predict. There can be no assurance that we would be able to locate alternative providers of such services, or that we could do so at economical rates.

We may be unable to adequately protect our intellectual property or rights to licenses for use of third-party intellectual property, and may be subject to claims that we infringe the intellectual property of others, which could substantially harm our business.

We rely on a combination of patents, copyrights, and other proprietary technology that we license from third parties. We have been issued several United States and foreign trademarks and may consider filing for additional trademarks in the future. We have also been issued one United States patent and may consider filing for additional patents in the future. However, we cannot assure you that any additional patents or trademarks will issue or that our issued patent or trademarks will be upheld in all cases. We cannot guarantee that these and other intellectual property protection measures will be sufficient to prevent misappropriation of our trademark or technology or that our competitors or licensors will not independently develop technologies that are substantially equivalent to or superior to ours. In addition, the legal systems in many other countries do not protect intellectual property rights to the same extent as the legal system of the United States. If we are unable to adequately protect our proprietary interests and business information or our present license arrangements, our business, financial condition and results of operations could be adversely affected. Further, the dependence of the telecommunications industry on proprietary technology has resulted in frequent litigation based on allegations of the infringement of patents and other intellectual property. In the future, we may be subject to litigation to defend against claimed infringement of the rights of others or to determine the scope and validity of the proprietary rights of others. Future litigation also may be necessary to enforce and protect our trade secrets and other intellectual property rights. Any intellectual property litigation could be costly and cause diversion of our management's attention from the operation of our business. Adverse determinations in any litigation could result in the loss of proprietary rights, subject us to significant liabilities or require us to seek licenses from third parties that may be available on commercially reasonable terms, if at all. We could also be subject to court orders preventing us from providing certain services in connection with the delivery of our services to our customers.

We experience turnover among our experienced and trained employee base, which could result in our inability to continue performing certain functions and completing certain initiatives in accordance with our existing budgets and operating plans.

We depend on the performance of our executive officers and key sales, engineering, and operations personnel, many of whom have significant experience in the telecommunications industry and substantial tenures with either our company or that of one of the companies that we have acquired. We experience turnover among our employees as a whole, and if we are not able to retain our executive officers or other key employees, we could experience a material and adverse effect on our financial condition and results of operations. In addition, in spite of the recent downturn in the U.S. economy, recruitment and retention of qualified employees remain highly competitive, and there can be no assurance that, if we lose one or more of our senior executives or key employees, we will be able to replace those persons, or, if we are able to replace such persons, that we will be able to do so without incurring significant additional labor costs or disruptions in our operations.

Several customers account for a significant portion of our revenue, and some our customer agreements may not continue due to bankruptcies, acquisitions, nonrenewal, or other factors.

We have substantial business relationships with large telecommunications carriers for whom we provide long distance and local transport services. The highly competitive environment and the industry consolidation in the long distance and wireless markets has challenged the financial condition and growth prospects of some of our carrier customers, and has caused such carrier customers to optimize the telecommunications capacity that they utilize among competing telecommunications services providers' networks, including ours. Replacing this revenue may be difficult because individual enterprise and SMB customers tend to place smaller service orders than our larger carrier customers. In addition, pricing pressure on products that we sell to our carrier customers may challenge our ability to grow revenue from carrier customers. As a result, if our larger carrier customers terminate the services they receive from us, our revenues and results of operations could be materially and adversely affected.

Risks Related to Competition and Our Industry

Technological advances and regulatory changes are eroding traditional barriers between formerly distinct telecommunications markets, which could increase the competition we face and put downward pressure on prices, which could impair our results.

New technologies, such as VoIP, and regulatory changes — particularly those permitting ILECs to provide long distance services — are blurring the distinctions between traditional and emerging telecommunications markets. In addition, the increasing importance of data services has focused the attention of most telecommunications companies on this growing sector. As a result, a competitor in any of our business areas is potentially a competitor in our other business areas, which could impair our prospects, put downward pressure on prices and adversely affect our operating results.

The telecommunications industry is highly competitive, and has experienced the consolidation of many existing competitors and the introduction of significant new competitors.

The communications industry is highly competitive. Many of our competitors generate significantly greater revenue, and possess significantly greater assets and financial resources than we do. In addition, if the business combinations involving SBC and AT& T, and either Verizon or Qwest and MCI that have been announced to date are consummated, those businesses as combined will enable SBC and Verizon or Qwest to offer the same or similar network reach as we do, and enable those companies to more effectively target the potential customers that are the focus of our business. This competition places downward pressure on prices for local and long distance telephone service and data services, which can adversely affect our operating results. Also, as the technology to deliver VoIP services is improved, more companies will be able to compete with us in our metro markets without constructing or acquiring PSTN assets in those markets. In addition, we could face competition from other companies, such as other competitive carriers, cable television companies, microwave carriers, wireless telephone system operators and private networks built by large end-users. We are much smaller in size and resources than many of our competitors. If we are not able to successfully compete against our larger competitors and the new entrants into the telecommunications market, our financial condition and results of operations could be materially and adversely affected.

Our company and industry are highly regulated, which restricts our ability to compete in our target markets and imposes substantial compliance costs on us that adversely impact our results.

We are subject to varying degrees of regulation from federal, state and local authorities. This regulation imposes substantial compliance costs on us. It also restricts our ability to compete. For example, in each state in which we desire to offer our services, we are required to obtain authorization from the appropriate state commission. If any required authorization for any of our markets or services is revoked or otherwise terminated, our ability to operate in the affected markets would be adversely affected.

Attempts to limit the basic competitive framework of the Telecom Act could interfere with the successful implementation of our business plan.

Successful implementation of our business plan is predicated on the assumption that the basic framework for competition in the local exchange services market established by the Telecom Act will remain in place. We expect that there will be attempts to limit or eliminate this basic framework through a combination of federal legislation, new rulemakings by the FCC and ILEC challenges to existing and proposed regulations. It is not possible to predict the nature of any such action or its impact on our business and operations.

Risks Related to Our Common Stock

An entity owned and controlled by Mr. Carl C. Icahn is our majority stockholder.

An entity owned and controlled by Mr. Carl C. Icahn, Chairman of our board of directors, has filed a Form 13D with the Securities and Exchange Commission in August 2004 disclosing that his beneficial ownership, as defined therein, was 60.7% of XO. As a result, Mr. Icahn has the power to elect all of our directors. Under applicable law and our certificate of incorporation and by-laws, certain actions cannot be taken without the approval of holders of a majority of our voting stock including, without limitation, mergers and the sale of substantially all of our assets and amendments to our certificate of incorporation and by-laws.

Future sales or issuances of our common stock could adversely affect its price and/or our ability to raise capital.

Future sales of substantial amounts of our common stock, or the perception that such sales could occur, could adversely affect the prevailing market price of our common stock and our ability to raise capital. In particular, we anticipate that the ATLT holder of approximately 45,380,000 shares of our common stock, may exercise its rights under an existing Registration Rights Agreement with us to cause us to file a registration statement to register the public resale of some or all of those shares.

As of March 14, 2005, there were 181,933,035 shares of our common stock outstanding. The shares of our common stock owned by an entity owned and controlled by Mr. Icahn are restricted shares that may be sold only under a registration statement or an exemption from federal securities registration requirements. Mr. Icahn, through various entities that he owns or controls, has the right to require XO to register, under the Securities Act of 1933, shares of common stock held by such entities and to include shares of our common stock held by them in certain registration statements filed by XO.

We have issued and there remain outstanding three series of warrants to purchase up to an aggregate of approximately 9.5 million, 7.1 million and 7.1 million additional shares of our common stock, at exercise prices of $6.25, $7.50 and $10.00 per share, respectively. The warrants will expire on January 16, 2010.

We have options outstanding to purchase approximately 11.3 million shares of common stock reserved for issuance under our 2002 Stock Incentive Plan as of December 31, 2004. Unless surrendered or cancelled earlier under the terms of the stock incentive plan, those options will expire beginning in 2013. In addition, our 2002 Stock Incentive Plan authorizes future grants of options to purchase common stock, or awards of restricted common stock, with respect to an additional 6.3 million shares of common stock in the aggregate.

Forward-Looking Statements

Our forward-looking statements are subject to a variety of factors that could cause actual results to differ significantly from current beliefs.

Some statements and information contained in this Annual Report on Form 10-K are not historical facts, but are "forward-looking statements," as such term is defined in the Private Securities Litigation Reform Act of 1995. These forward-looking statements can be identified by the use of forward-looking terminology such as "believes," "expects," "plans," "may," "will," "would," "could," "should," or "anticipates" or the negative of these words or other variations of these words or other comparable words, or by discussions of strategy that involve risks and uncertainties. Such forward-looking statements include, but are not limited to, statements regarding:

- our services, including the development and deployment of data products and services based on IP, Ethernet and other technologies and strategies to expand our targeted customer base and broaden our sales channels;
- the operation of our network, including with respect to the development of IP protocols;
- liquidity and financial resources, including anticipated capital expenditures, funding of capital expenditures and anticipated levels of indebtedness; and
- trends related to and expectations regarding the results of operations in future periods, including but not limited to those statements set forth in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations below.

All such forward-looking statements are qualified by the inherent risks and uncertainties surrounding expectations generally, and also may materially differ from our actual experience involving any one or more of these matters and subject areas. The operation and results of our business also may be subject to the effect of other risks and uncertainties, in addition to the relevant qualifying factors identified in the above "Risk Factors" section and elsewhere in this annual report and in the documents incorporated by reference in this annual report, including, but not limited to:

- general economic conditions in the geographic areas that we are targeting for communications services;
- the ability to achieve and maintain market penetration and average per customer revenue levels sufficient to provide financial viability to our business;
- the quality and price of similar or comparable communications services offered or to be offered by our current or future competitors; and
- future telecommunications-related legislation or regulatory actions.

Item 2. Properties

We own or lease, in our operating territories, telephone property which includes: fiber optic backbone and distribution network facilities; wireless distribution sites; central office switching equipment; connecting lines between customers' premises and the central offices; and customer premise equipment. Our central office switching equipment includes electronic switches and peripheral equipment.

The fiber optic backbone and distribution network and connecting lines include aerial and underground cable, conduit, poles and wires. These facilities are located on public streets and highways or on privately-owned land. We have permission to use these lands pursuant to consent or lease, permit, easement, or other agreements.

We lease facilities for our administrative and sales offices, central switching offices, network nodes and warehouse space. The various leases expire in years ranging from 2005 to 2029. Most have renewal options.

Our headquarters are located in Reston, Virginia, where we are currently leasing approximately 170,000 square feet of space. In February 2003, Dixon Properties, LLC, which is owned by Mr. Carl Icahn, acquired ownership of the building in which our headquarters is located in a transaction that was approved by the Bankruptcy Court in our Chapter 11 proceedings.

Item 3. Legal Proceedings

XO is involved in lawsuits, claims, investigations and proceedings consisting of commercial, regulatory, securities, tort and employment matters, which arise in the ordinary course of business. In accordance with SFAS No. 5, "Accounting for Contingencies," XO makes a provision for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. XO believes it has adequate provisions for any such matters. XO reviews these provisions at least quarterly and adjusts these provisions to reflect the impacts of negotiations, settlements, rulings, advice of legal counsel, and other information and events pertaining to a particular case. Litigation is inherently unpredictable. However, XO believes that it has valid defenses with respect to legal matters pending against it. Nevertheless, it is possible that cash flows or results of operations could be materially affected in any particular period by the unfavorable resolution of one or more of these contingencies.

XO filed an administrative claim in August 2004 against the ATLT. XO has claimed that it is entitled to approximately $50 million in damages related to a variety of actions allegedly taken by Allegiance and the ATLT. The ATLT filed a counterclaim against XO on November 24, 2004 seeking damages of approximately $100 million, which claim XO believes to be frivolous and without merit. This action is pending in the U.S. Bankruptcy Court for the Southern District of New York.

In addition, disputes with respect to general unsecured claims and one administrative claim against XO in the amount of approximately $2.1 million, remain pending from the XO's 2002 Chapter 11 proceedings.

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

No matter was submitted to a vote of security holders during the fourth quarter.

Part II

Item 5. Market for Registrant's Common Equity and Related Stockholder Matters and Issuer Purchases of Equity Securities

Our common stock is quoted on the OTCBB under the symbol "XOCM.OB." According to the records of our transfer agent, we had 68 stockholders of record as of March 14, 2005. The majority of our shares that are held by non-affiliates are held in approximately 35,000 customer accounts held by brokers and other institutions on behalf of stockholders. The following table sets forth the low and high sale price of our common stock, based on the last daily sale, in each of our last eight fiscal quarters.

	2004		2003	
	High	Low	High	Low
First Quarter	$ 7.90	$ 4.98	$ 4.00	$ 0.35
Second Quarter	$ 5.70	$ 3.33	$ 7.80	$ 3.90
Third Quarter	$ 4.00	$ 3.16	$ 8.33	$ 5.60
Fourth Quarter	$ 3.62	$ 2.67	$ 5.80	$ 4.97

All of the 2004 over-the-counter market quotations set forth in this table reflect inter-dealer quotations, without retail mark-up, mark-down, or commission and may not necessarily reflect actual transactions. Our Credit Facility prohibits the payment of cash dividends.

Item 6. Selected Financial Data

Our selected financial data table follows (dollars in thousands, except share data).

	Reorganized XO(f)		Predecessor XO(f)		
	Year Ended December 31,		Year Ended December 31,		
	2004(a)	2003	2002	2001	2000
Statement of Operations Data:					
Revenue	$ 1,300,420	$ 1,110,483	$ 1,259,853	$ 1,258,567	$ 723,826
Loss from operations (b)	(370,292)	(111,858)	(1,208,898)	(1,949,891)	(1,011,652)
Net loss (c)	(405,543)	(102,554)	(3,386,818)	(2,086,125)	(1,101,299)
Net loss applicable to common shares (c)(d)	(410,453)	(102,554)	(3,350,362)	(1,838,917)	(1,247,655)
Net loss per common share, basic and diluted	(2.57)	(1.07)	(7.58)	(4.55)	(3.87)
Statement of Cash Flow Data:					
Net cash (used in) provided by operating activities	$ 150	$ 6,301	$ 17,602	$ (560,877)	$ (559,414)
Net cash (used in) provided by investing activities	(444,837)	153,036	57,582	(708,598)	(1,464,495)
Net cash (used in) provided by financing activities	200,116	5,185	(6,079)	(1,019,647)	1,648,663
Balance Sheet Data:					
Cash, cash equivalents and marketable securities	$ 251,289	$ 520,612	$ 560,983	$ 755,167	$ 1,860,963
Property and equipment, net	820,536	485,984	2,780,589	3,742,577	2,794,105
Broadband wireless licenses and other intangibles, net (c)	139,866	109,515	984,614	2,977,575	3,912,209
Total assets (c)	1,459,385	1,265,165	4,585,496	7,930,465	9,085,375
Total long-term debt and accrued interest payable (e)	366,247	536,791	5,165,718	5,109,503	4,396,596
Redeemable preferred stock, net of issuance costs	204,353	—	1,708,316	1,781,990	2,097,016
Total stockholders' equity (deficit) (e)	485,552	380,425	(3,032,282)	297,416	1,838,401

(a) The selected consolidated financial data includes the accounts and activities of the businesses we acquired from Allegiance Telecom, Inc. from June 23, 2004, the acquisition date through December 31, 2004.

(b) In 2004, loss from operations included a $212.5 million non-cash impairment charge of goodwill. In 2002, loss from operations included non-cash charges totaling $477.3 million in connection with the amendment to the terms of fiber acquisition and maintenance arrangements with Level 3 Communications, and the return of previously acquired intercity fiber in connection therewith. In 2001, loss from operations included restructuring charges totaling $509.2 million associated with the restructuring of certain aspects of our business operations. Loss from operations in 1999 included restructuring charges totaling $30.9 million associated with relocating our Bellevue, Washington headquarters to Reston, Virginia.

(c) In 2004, net loss included a $212.5 million non-cash impairment charge of goodwill. In 2003, net loss included a $33.5 million gain on investment sales. In 2002, net loss and total assets reflects a $1,876.6 million impairment charge to write-off all of our goodwill as a cumulative effect of accounting change, pursuant to SFAS No. 142. In 2001, net loss included a gain of $345.0 million resulting from the repurchase of certain of our senior notes. In 2000, net loss included a $225.1 million net gain from the sale of an equity investment.

(d) The comparability of net loss applicable to common shares is impacted by the transactions discussed in c. above. In 2001, net loss applicable to common shares includes a gain of $376.9 million resulting from the repurchase of certain of our preferred stock.

(e) In January 2004, we completed a rights offering. An aggregate of 39.7 million shares were issued in the offering, yielding net proceeds of $197.6 million. These proceeds were used to pay down our long-term debt and accrued interest payable.

(f) The reorganized selected consolidated financial data as of and for the years ended December 31, 2004 and 2003 reflects the impact of adopting fresh start as of January 1, 2003, and is not comparable to that of predecessor XO. The predecessor selected consolidated financial data below as of and for the years ended December 31, 2002, 2001, and 2000 does not include the effects of the fresh start accounting provisions of SOP 90-7. Fresh start required that XO adjust the historical cost of its assets and liabilities to their fair values as determined by the reorganization value of the Company.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Executive Overview of Our Business

State of the Telecommunications Industry

In general, growth in the telecommunications industry has been sluggish for the past three years. Demand for some services, such as wireless and integrated product offerings has increased, but for many other products and services price compression, reductions in regulated rates and lower demand have resulted in year over year revenue declines for many telecommunication companies. As a result our industry has seen:

- Reduced new customer demand and/or reductions in existing customer services,
- High number of bankruptcies in the telecommunications industry and the economy in general,
- Continued competitive pressures, including price cutting in some product lines,
- Mandated FCC carrier access rate reductions.

Aggregate revenue earned from the sale of wired telecommunications services in 2004 has been estimated at approximately $225 billion, down approximately three percent from 2003. Telecommunications sales to business customers, however, is estimated to have remained relatively constant at $91 billion, with sales of local exchange services estimated to have increased by approximately one percent to approximately $42.5 billion in 2004 compared to 2003. Telecommunications spending by businesses who spend less that $10,000 per month or SMBs, was estimated to be $75 billion in 2004.

The telecommunications industry currently remains in a state of competitive transition as the combination of new federal and state regulations, industry consolidation, emergence of new technologies, growth of the mobile wireless market, and entry of new telecommunications competitors, such as cable television companies, has contributed to a rapidly changing market for telecommunications services.

Business Overview

We provide a comprehensive array of telecommunications services to business customers. We provide our services, including local and long distance voice, Internet access, private data networking and hosting services, through our national telecommunications network, which consists of more than 6,700 route miles of fiber optic lines connecting 953 unique ILEC end-office collocations in 37 U.S. cities. In addition, we own licenses to deliver telecommunications services via local, multipoint distribution service, or LMDS, wireless spectrum in all of the largest U.S. cities. We market our services primarily to business customers, ranging from small and medium businesses to Fortune 500 companies to carrier and wholesale customers. Our services offer an effective telecommunications solution for nearly any business, and our national telecommunications network is particularly advantageous to multi-location businesses that desire to improve communications among their locations, whether within a single metropolitan area or across the country.

Key Performance Indicators

Management uses various key performance indicators, or KPIs, to assess operational effectiveness in certain areas. These include:

- Revenue Growth — This KPI tracks a combination of sales trends, pricing strategy and operational effectiveness.
- Operating expenses as a percentage of revenue — This KPI tracks our efficiencies in providing services and our profitability.
- Customer attrition or churn — This KPI tracks the financial impact of customer attrition, or churn, in comparison to new sales. Management reviews this KPI to judge the effectiveness of operational measures intended to promote customer retention and satisfaction with our services, and the net impact on revenue.

System Conversions

During 2004, we continued to invest capital into the development and implementation of our information systems that increase revenue and/or improve our customer's experience, and/or increase productivity.

- XO has completed a number of systems initiatives that improved our sales operations and customer service, including:
  - A customer and prospect management system to facilitate the handling of customer and prospect leads;
  - A network pricing tool to facilitate production of price quotes for the sales team;
  - A project integration tool to allow cross selling of XO products by Allegiance sales personnel and the reverse;
  - A vendor and customer referral tool for lead generation; and
  - An ordering system for the selling of the first XO VoIP product, XOptions Flex.
- In order to improve productivity through the automation of business processes, we focused on improving the order installation process by implementing systems initiatives including:
  - An electronic bonding system for trouble ticketing and order management between XO and several ILECs;
  - A new ordering platform to enable standardized selling processes;
  - An order flow through from our order entry system to our provisioning and billing systems for XO's four key products;
  - An Automated Switch Translation system, which automated the interface between the provisioning systems and the network elements; and
  - A new Workforce Management system with full integration between the Workforce Management system and provisioning and trouble ticketing.
- In addition, to improve productivity and to take advantage of the combination of the Allegiance and XO assets, XO assessed the capabilities of both systems' portfolios and delivered a combined architecture, leveraging the best systems while reducing overall cost. Systems that have been consolidated include:
  - Network monitoring systems,
  - Virus management systems,

- General Ledger and Accounts Receivable systems,
- Human Resource systems,
- Sales commission systems,
- Telco cost management platforms,
- Carrier Access Billing systems,
- Payroll systems,
- Time and attendance systems, and
- Call Management systems.

Other 2004 Transactions and Developments

Acquisition of Assets of Allegiance Telecom, Inc.

On June 23, 2004, we acquired the telecommunication services of Allegiance Telecom, Inc., or Allegiance, for approximately $325.2 million in cash and approximately 45.38 million shares of our common stock. After the acquisition, XO became one of the nations' largest competitive providers of national local telecommunications and broadband services with approximately $1.5 billion in pro forma annual revenues. We currently own one of the largest network of nationwide connections to the ILEC's networks, and doubled our collocations within the 36 metropolitan areas where we operate.

As of December 31, 2004, we have completely integrated the administrative functions of XO and Allegiance and have achieved all of the originally estimated $100 million of annualized synergies. We have made substantial progress in achieving the originally estimated $60 million of annualized network synergies. We have connected all of the former Allegiance collocations, allowing us to carry traffic across the combined XO and Allegiance networks. We have also integrated many administrative systems and contracts and have reduced the aggregate workforce of the combined companies from over 7,000 as of January 1, 2004 to approximately 5,000 as of December 31, 2004.

After the Closing Date, Allegiance transferred the remaining assets that XO did not buy to the ATLT. XO filed an administrative claim in August 2004 against the ATLT. XO has claimed that it is entitled to approximately $50 million in damages related to a variety of actions allegedly taken by Allegiance and the ATLT. The ATLT filed a counterclaim against XO on November 24, 2004 seeking damages of approximately $100 million, which claim XO believes to be frivolous and without merit. The accompanying financial statements do not include any financial impact from this litigation as it is too early in the process to assess any outcome. This action is pending in the U.S. Bankruptcy Court for the Southern District of New York.

Convertible Preferred Stock

On August 6, 2004, XO completed a private placement of 4.0 million shares of its 6% Class A Convertible Preferred Stock (the "Preferred Stock Offering") for net proceeds of $199.4 million. Affiliates of Mr. Icahn purchased 95% of the preferred shares sold in the Preferred Stock Offering, and an affiliate of Amalgamated Gadget, L.P., holder of approximately 8% of XO's outstanding common stock, purchased the remaining five percent.

The Preferred Stock Offering was reviewed and approved by a special committee of XO's Board of Directors consisting of XO's three independent directors, Messrs. Dell, Gradin and Knauss. The special committee selected its own counsel and financial advisor. The financial advisor advised the special committee that, subject to specified qualifications, assumptions and limitations, the material terms of the 6% Class A Convertible Preferred Stock were fair to XO, from a financial point of view, at the time of issuance. Proceeds of the Preferred Stock Offering will be used for general working capital purposes and to fund possible future acquisitions that would add additional scale and synergies to XO's business.

Liquidity and Capital Resources

Capital Resources and Liquidity Assessment

Our cash and cash equivalents decreased from $478.6 million at December 31, 2003, to $234.0 million at December 31, 2004 largely due to our acquisition of Allegiance's telecommunications services assets which included a cash payment of $325.2 million. Other significant liquidity events during the year included raising capital through the issuance of common stock under a rights offering that provided net proceeds of $197.6 million, and the issuance of preferred stock that provided net proceeds of $199.4 million. In addition, we paid down $199.7 million of principal outstanding under our Credit Facility and capital leases during the year, and invested $106.0 million of capital into our telecommunications network and information systems. Our operating activities provided net cash of $0.2 million during 2004. This is largely due to the growth in revenue and the improvement of selling, operating and general expenses as a percentage of revenue due to the synergies achieved after the acquisition of Allegiance's telecommunications services assets.

Our Credit Facility includes a financial covenant requiring us to maintain minimum earnings before interest, taxes, depreciation, and amortization, or EBITDA, for the twelve-month period ending each fiscal quarter. We did not meet this covenant in 2004 and based on current financial results, we do not expect to comply with this covenant in 2005. We have obtained a waiver through December 31, 2005. If we are not able to (i) amend this Credit Facility covenant to either remove the minimum EBITDA requirements or to decrease the requirement to a level we believe we can achieve, (ii) obtain an extension on the waiver to at least March 31, 2006, or (iii) repay the Credit Facility with a new debt or equity offering, under the current accounting guidelines we will be required to reclassify the $366.2 million amount outstanding from long term to short term as of March 31, 2005. While the existing waivers prevent the lenders under the Credit Facility from accelerating repayment of the outstanding indebtedness under the Credit Facility until March 31, 2006, this reclassification would cause a significant deterioration to our disclosed working capital and financial position.

There are no additional borrowings available under our Credit Facility. We have no current debt service requirements since cash interest payments as well as automatic and permanent quarterly reductions of the principal amount outstanding under the Credit Facility do not commence until 2009. However, in the event that consolidated excess cash flow (as defined in the Credit Facility) for any fiscal quarter during the term of the agreement is greater than $25 million, at the request of the lender, XO will pay an amount equal to 50% of such excess cash flow greater than $25 million toward the reduction of outstanding indebtedness. In addition, if the ratio of our consolidated earnings before interest, taxes depreciation and amortization to consolidated interest expense for the four consecutive quarters exceeds 4:1, we would be required to pay cash interest, unless waived by the lenders.

We project that we will make significant progress on our operating results such that we will be cash flow positive in 2005 and that in late 2005 we will be able to fund our capital expenditures from operating cash flows. Our projection is based upon our current estimates of, among other things, our estimated increased costs of service attributable to the recent TRRO and other projected operating costs that are not entirely in XO's control. As a result, our 2005 projections may not prove to be correct if our estimates of such costs and expenses are inaccurate. In addition, our ability to remain cash flow positive over the longer term is dependent on our ability to extend the waiver of our existing senior debt covenants, refinance our existing senior debt, or repay that senior debt from then-existing cash reserves.

We expect that the majority of our planned capital expenditures will be "success based" in that they will be used to grow revenue by purchasing and installing customer-related equipment and network electronics for either new customers or by adding services provided to existing customers. Much of our non-success based capital will be for the continued development and implementation of our information systems in support of new product introductions, cost management, continued automation of XO's business processes, and continued integration of XO's and Allegiance's information systems.

Our national network requires various ongoing maintenance costs and software licenses and fees so that we can continue to provide high quality telecommunication services to our customers. Where we do not have our own network to provide telecommunication services we pay access rights and use fees to other service providers. To achieve the most cost efficient rates, we often commit to a multi year purchase for these services and licenses. The Company is leasing premises under various noncancelable operating leases for administrative space, building access, and other 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 2029. The following table summarizes our payment obligations under various operating and financing agreements as of December 31, 2004 (dollars in thousands):

Year Ending December 31,	Credit Facility	Other long-term contractual obligations	Operating lease obligations	Capital lease obligations	Total obligations
2005	$ —	$ 61,273	$ 70,822	$ 4,789	$ 136,884
2006	—	52,521	66,657	4,537	123,715
2007	—	48,806	61,527	3,854	114,187
2008	—	47,524	51,394	2,398	101,316
2009	366,247	33,679	43,257	1,770	444,953
Thereafter	—	95,787	168,235	13,681	277,703
Total minimum commitments	$366,247	$ 339,590	$ 461,892	$ 31,029	$ 1,198,758

As discussed in Part I, Item 1, Business, we prepaid to lease wavelength capacity from Level 3 for intercity network capacity. The leases expire in 2006 and 2007. At that time, we will either renew these leased wavelengths at current market rates or install our own optical equipment and light certain segment routes of our intercity fiber network, either of which will be a substantial capital commitment.

If we successfully either, extend the waivers for the financial covenants or renegotiate or refinance the Credit Facility as discussed above, we expect that our current cash balance will allow us to successfully execute our current business plan. Current economic conditions of the telecommunications industry may create opportunities for us acquire on other companies or portions of companies at attractive prices. We expect to continue to pursue the acquisition of additional telecommunication companies or assets throughout 2005. We do not know what the terms of any such transactions would be. Any offers involving cash consideration could significantly and adversely affect our liquidity. To support further business expansion, including investments in or acquisitions of other companies or portion of other companies, we may issue additional equity and/or debt securities.

Comparison of Financial Results

The operational results for the year ended December 31, 2004 are discussed below. The 2004 amounts include the results of operations of the Allegiance telecommunication services assets, which we refer to as the Acquired Businesses from June 23, 2004 through December 31, 2004.

XO Year Ended December 31, 2004 Compared to Year Ended December 31, 2003

Revenue. Total revenue for the year ending December 31, 2004 increased 17.1% to $1,300.4 million from $1,110.5 million for the year ending December 31, 2003. The 2004 financial results include approximately $217.2 million of revenue from the Acquired Businesses. Without the revenue from the Acquired Businesses our 2004 revenue decreased $27.3 million or 2.5% from 2003 results. Customer churn and continued pricing pressures, particularly in carrier long distance, offset revenue growth from new customers. Customer churn is driven by a highly competitive environment, large customers downsizing their telecom needs, and finally our deemphasizing of products like DSL, Hosting and Dial-up allowing our sales resources to focus on larger customers and products. We expect 2005 annualized revenue to be consistent with our fourth quarter 2004 results.

Revenue was earned from providing the following services (dollars in thousands):

	Year Ended December 31,		Year Ended December 31,		
	2004	% of 2004 Revenue	2003	% of 2003 Revenue	% Change
Voice services	$ 673,318	51.8%	$ 572,774	51.6%	17.6%
Data services	414,782	31.9%	392,742	35.4%	5.6%
Integrated voice and data services	212,320	16.3%	144,967	13.0%	46.5%
Total revenue	$ 1,300,420	100.0%	$ 1,110,483	100.0%	17.1%

Voice services revenue includes revenue from local and long distance voice services, prepaid calling card processing, interactive voice response services, stand-alone long distance services and other voice telecommunications based services. Our 2004 results include approximately $127.0 million of voice services revenue from the Acquired Businesses. Voice services revenue for the year ended December 31, 2004 exclusive of voice services revenue from the Acquired Businesses, decreased $26.5 million or 4.6% from 2003 results. The decrease is attributable to customer churn, competitive pricing pressures, particularly long distance, and reduced FCC mandated rates.

Data services revenue includes revenue from Internet access, network access and web applications hosting services. Our 2004 results include approximately $32.2 million of data services revenue from the Acquired Businesses. Data services revenue for the year ended December 31, 2004 exclusive of data services revenue from the Acquired Businesses decreased $10.1 million or 2.6% from 2003 results. The decrease was attributable to an increase in customer churn due to network downsizing from high end customers and our deemphasizing certain less profitable products such as DSL, dial up, and hosting services.

Integrated voice and data services revenue is attributed to our XOptions and Total Communications service offerings, XO's flat-rate bundled packages offering a combination of voice and data services and integrated access. Our 2004 results include approximately $58.0 million of integrated voice and data services revenue from the Acquired Businesses. Integrated voice and data services revenue for the year ended December 31, 2004 exclusive of services revenue from the Acquired Businesses increased $9.3 million or 6.4% from 2003 results due to growth in our integrated access services, as well as our XOptions service offering.

Costs and expenses. The table below provides costs and expenses by classification and as a percentage of revenue (dollars in thousands). Our consolidated costs and expenses in 2004 include the costs to run the Acquired Businesses since June 23, 2004.

	Year Ended December 31,		Year Ended December 31,		
	2004	% of 2004 Revenue	2003	% of 2003 Revenue	% Change
Costs and expenses:					
Cost of service	$ 552,735	42.5%	$ 422,129	38.0%	30.9%
Selling, operating and general	727,666	56.0%	679,286	61.2%	7.1%
Depreciation and amortization	177,781	13.7%	109,308	9.8%	62.6%
Goodwill impairment charge	212,530	16.3%	—	0.0%	100.0%
Restructuring and asset write-downs	—	0.0%	11,618	1.1%	(100.0%)
Total	$ 1,670,712	128.5%	$ 1,222,341	110.1%	36.7%

Cost of service. Cost of service includes expenses directly associated with providing telecommunications services to our customers. Cost of service includes, among other items, the cost of connecting customers to our networks via leased facilities, the costs of leasing components of our network facilities and costs paid to third party service providers for interconnect access and transport services. Cost of service as a percentage of revenue for the year ended December 31, 2004 increased as compared to the same period in 2003 due to the impact of pricing pressures from both mandated FCC carrier access rate reductions and general pricing reductions on revenue, as well as an unfavorable shift in traffic mix for terminations, offset by savings from synergies associated with the integration of the Acquired Business.

We believe that cost of service as a percentage of revenue in 2005 for the combined companies will remain relatively stable with 2004 results. However, cost of service in both absolute dollars and as a percentage of revenue may be adversely impacted due to recently proposed regulatory rules on UNE loop and transport rates as discussed in the "Regulatory Overview" section in Part I, Item 1. Our current estimates project an annualized increase of approximately $45 million due to these regulatory changes. These increases will be phased in during 2005, and be fully implemented by 2006. We believe that we should be able to recover the majority of these cost increases through network optimization, and price increases throughout our markets.

We originally estimated a potential benefit of approximately $60.0 million in pro forma annualized network synergies for the combined companies if our integration efforts with the Acquired Businesses were successful. We have made substantial progress integrating the two companies and are on plan to achieve this target.

Selling, operating and general. Selling, operating and general expense includes expenses related to network maintenance, sales and marketing, network operations and engineering, information systems, general corporate office functions and collection risks. Selling, operating and general expense for the year ended December 31, 2004 was $727.7 million or 56.0% of revenue versus $679.3 million or 61.2% of revenue for the year ended December 31, 2003. The decrease in selling, operating and general expense as a percentage of revenue for the year ended December 31, 2004 when compared to 2003 results is due to the achievement of synergies related to the Acquired Businesses. Our fourth quarter 2004 results are reduced due to favorable settlements for $11.9 million.

We believe that, selling, operating and general expense will decrease as a percentage of revenue in 2005 when compared with 2004 results. We originally estimated a potential benefit of approximately $100.0 million in pro forma annualized selling, operating and general expense synergies for the combined companies if our integration efforts with the Acquired Businesses were successful. We have completely integrated the administrative functions and have achieved all of the estimated annualized synergies.

Depreciation and amortization. Depreciation and amortization expense was $177.8 million for the year ended December 31, 2004, and $109.3 million for the year ended December 31, 2003. The increase is largely due to the inclusion of fixed assets and intangibles of the Acquired Businesses.

As of December 31, 2004, we had approximately $115.9 million of fixed assets and $23.5 million of broadband wireless licenses that have not yet been placed into service and, accordingly, are not currently being depreciated or amortized. We expect depreciation and amortization expense during 2005 to increase as additional assets are placed into service and as we recognize a full year of depreciation and amortization of the assets of the Acquired Businesses.

Goodwill impairment charge. We retained independent appraisers to perform a preliminary valuation of our assets and liabilities as of December 31, 2004. This valuation was necessary as our fair value as determined by our stock price, was less than our book value. Based on this appraisal we recorded a $212.5 million non-cash impairment charge on our goodwill.

Restructuring and asset write-downs. Restructuring and asset write-downs were $11.6 million for the year ended December 31, 2003. Restructuring charges in 2003 included costs for a reduction in our workforce by approximately 550 employees and estimated losses associated with restructured leases.

Investment income, net. Investment income, net includes interest income as well as any realized gains or losses from the sale of investments. Investment income, net was a loss of $9.0 million and a net gain of $46.2 million in 2004 and 2003, respectively. The 2004 balance includes a $10.4 million impairment adjustment on an investment, that was considered to be other than temporary. The 2003 balance is primarily from a gain on the sale of an investment.

Interest expense, net. Interest expense, net includes interest expense on debt and capital leases, less any amounts capitalized. The majority of interest expense in 2004 and 2003 is non-cash as our Credit Facility allows for accrued interest to be converted into principal if unpaid. Interest expense, net for the years ended December 31, 2004 and 2003 was $26.2 million and $36.8 million, respectively. The significant reduction for 2004 was due to a $197.6 million repayment of outstanding principal under the Credit Facility in January 2004. During 2004 and 2003, XO capitalized interest of $4.0 million and $3.0 million, respectively.

Reorganized XO Year Ended December 31, 2003 Compared to Predecessor XO Year Ended December 31, 2002

As a consequence of our Chapter 11 reorganization, the financial results for the year ended December 31, 2003 have been separately presented under the label "Reorganized XO" and are not comparable with prior year results. The reorganized Company has adopted the policy of expensing customer installation costs in the period in which the costs are incurred. The predecessor Company capitalized and amortized these costs. In accordance with SOP 90-7, the reorganized Company was required to implement newly issued accounting pronouncements that would require adoption within twelve months of applying fresh start.

Revenue. Total revenue for the year ending December 31, 2003 decreased 11.8% to $1,110.5 million from $1,259.9 million for the year ending December 31, 2002. Customer churn, of approximately 2.4% in 2003, exceeded acquisition revenue particularly in the carrier, stand alone, DSL and dial-up customer base. The majority of this decline is driven by major reductions in the carrier revenue stream due to bankruptcies, downsizing network requirements, as well as competitive pricing pressures. Additionally, year-over-year revenue decreased in ancillary stand alone products such as Dial Up and DSL Internet access, and Hosting due to XO focusing on more profitable offerings. The commercial offerings to middle market businesses, however, remained relatively stable as revenue acquisition kept pace with attrition.

Revenue was earned from providing the following services (dollars in thousands):

	Reorganized XO Year Ended December 31,		Predecessor XO Year Ended December 31,		
	2003	% of 2003 Revenue	2002	% of 2002 Revenue	% Change
Voice services	$ 572,774	51.6%	$ 659,558	52.3%	(13.2%)
Data services	392,742	35.4%	472,247	37.5%	(16.8%)
Integrated voice and data services	144,967	13.0%	128,048	10.2%	13.2%
Total revenue	$ 1,110,483	100.0%	$ 1,259,853	100.0%	(11.8%)

Voice services revenue includes revenue from local and long distance voice services, prepaid calling card processing, and other voice telecommunications based services, interactive voice response services and stand-alone long distance services. Voice services revenue for the year ended December 31, 2003 decreased to $572.8 million from $659.6 million for the same period of 2002. The decrease is attributable to reduced FCC mandated rates, price reductions in long distance services due to reduced cost of service due to technological improvements, and customer disconnects and usage reductions arising from customers' downsizing due to the state of the domestic economy.

Data services revenue includes revenue from Internet access, network access and web applications hosting services. Data services revenue for the year ended December 31, 2003 decreased to $392.7 million from $472.2 million for the same period of 2002. The decline was attributable to an increase in customer bankruptcies, and customer disconnects, and a lower demand from large customers due to reductions in those customers' data capacity needs.

Integrated voice and data services revenue is generated largely from our XOptions service offerings, a flat-rate bundled package offering a combination of voice and data services. Integrated voice and data services revenue for the year ended December 31, 2003 increased to $145.0 million from $128.0 million for the same period in 2002. The increase is due to the continued acceptance in the marketplace of our XOptions service offering.

Costs and expenses. The table below provides costs and expenses by classification and as a percentage of revenue (dollars in thousands):

	Reorganized XO Year Ended December 31,		Predecessor XO Year Ended December 31,		
	2003	% of 2003 Revenue	2002	% of 2002 Revenue	% Change
Costs and expenses:					
Cost of service	$ 422,129	38.0%	$ 522,924	41.5%	(19.3%)
Selling, operating and general	679,286	61.2%	765,853	60.8%	(11.3%)
Depreciation and amortization	109,308	9.8%	699,806	55.5%	(84.4%)
Restructuring and asset write-downs	11,618	1.1%	480,168	38.1%	(97.6%)
Total	$ 1,222,341	110.1%	$ 2,468,751	196.0%	(50.5%)

Cost of service. Cost of service includes expenses directly associated with providing telecommunications services to our customers. Cost of service includes, among other items, the cost of connecting customers to our networks via leased facilities, the costs of leasing components of our network facilities and costs paid to third party service providers for interconnect access and transport services. Cost of service for the year ended December 31, 2003 decreased in absolute dollars and as a percentage of revenue compared to the same period in 2002. The year over year decline as a percentage of revenue was due primarily to cost optimization programs which reduced expenses by transferring traffic from third party facilities onto our owned or controlled facilities, and favorable resolutions of disputed third party costs. The decline was partially offset by our adoption of an accounting policy during the first quarter of 2003, to expense rather than defer costs associated with the installation of customer services and the revenue reductions in carrier long-distance services due to the excess long haul capacity in the sector.

Selling, operating and general. Selling, operating and general expense includes expenses related to sales and marketing, internal network operations and engineering, information systems, general corporate office functions and collection risks. Selling, operating and general expense for the year ended December 31, 2003 was $679.3 million or 61.2% of revenue versus $765.9 million or 60.8% of revenue for the year ended December 31, 2002. Selling, operating and general expense decreased in absolute dollars due to our reorganization that resulted in reduced headcount, contract rejections and renegotiations, and fair value adjustments to our long term contractual commitments and property as required by fresh start accounting which resulted in expense reductions in various contracted services, rent and property taxes. These reductions were partially offset by our adoption of the policy of expensing internal labor costs directly associated with customer installation and the construction of our network. The increase in selling, operating and general expense as a percentage of revenue for the year ended December 31, 2003 when compared to 2002 results is due to the large reduction of revenues due to bankruptcies and price declines discussed above, with no associated offsetting direct expense reduction.

Depreciation and amortization. As discussed above, we implemented fresh start on January 1, 2003 and adjusted the carrying value of our property and equipment and other intangibles to their fair value which resulted in a significant reduction of the aggregate historical carrying value. Consequently, depreciation and amortization expense decreased to $109.3 million for the year ended December 31, 2003, versus $699.8 million for the year ended December 31, 2002.

Restructuring and asset write-downs. Restructuring and asset write-downs decreased to $11.6 million for the year ended December 31, 2003 from $480.2 million for the year ended December 31, 2002.

Restructuring charges in 2003 include costs for a reduction in our workforce by approximately 550 employees, primarily employed in network operations, sales and marketing and information technology and estimated losses associated with restructured leases.

The 2002 restructuring charges primarily include a $477.3 million non-cash asset write-down during the third quarter of 2002 as a result of returning intercity assets to Level 3 in exchange for reduced future maintenance expenses beginning in 2003.

Investment income (loss), net. Investment income (loss), net includes interest income as well as any realized gains or losses from the sale of investments. Investment income (loss), net was a gain of $46.2 million for 2003 and a gain of $16.3 million in 2002. The 2003 balance is primarily for a gain on the sale of an investment.

Interest expense, net. Interest expense, net includes interest expense on debt and capital leases, less any amounts capitalized for construction efforts. The majority of interest expense in 2003 is non-cash as the Credit Facility allows for accrued interest to be converted into principal if unpaid. Interest expense, net for the years ended December 31, 2003 and 2002 was $36.8 million and $226.5 million, respectively. During 2003 and 2002, XO capitalized interest of $3.0 million and $11.1 million, respectively. Contractual interest was $501.1 million for the year ended December 31, 2002. The significant reduction for 2003 was caused by the cancellation of our pre-petition senior notes and pre-petition convertible subordinated notes and the reduction in the amount outstanding under our Credit Facility upon consummation of our Plan of Reorganization.

Critical Accounting Policies and Estimates

The preparation of the consolidated financial statements in accordance with accounting principles generally accepted in the United States requires management to make judgments, estimates and assumptions regarding uncertainties that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. Management uses historical experience and all available information to make these judgments and estimates. Actual results could differ. Despite these inherent limitations, management believes that Management's Discussion and Analysis and the accompanying consolidated financial statements and footnotes provide a meaningful and fair perspective of our financial condition and our operating results for the current period. Management believes the following critical accounting policies represent the more significant judgments and estimates used in the preparation of our audited consolidated financial statements included in this form 10-K.

Business Combinations

Upon the Closing Date, XO acquired title to the Acquired Businesses. XO retained independent appraisers to determine the fair value of the property, plant and equipment and intangible assets acquired as required under SFAS No. 141. The following are the estimated fair value of assets acquired and liabilities assumed (dollars in thousands):

Current assets	$ 51,618
Property and equipment	372,405
Goodwill	212,530
Other intangible assets	68,052
Other long-term assets	2,933
Total assets acquired	707,538
Current liabilities	(58,193)
Long-term liabilities	(12,790)
Total liabilities acquired	(70,983)
Purchase price	$ 636,555

The values assigned in these financial statements are preliminary and represent management's best estimate of current values which are subject to revision due to changes in estimates of fair value as well as the pending claim discussed in Part I, Item 3 "Legal Proceedings." As required by the SFAS No. 142, we tested our goodwill for impairment at December 31, 2004 and recorded a non-cash impairment of $212.5 million. This is discussed in more detail in long-lived assets below.

Long-Lived Assets

Our long-lived assets include property and equipment, goodwill, broadband wireless licenses, and identifiable intangible assets to be held and used. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets. The estimated useful lives of telecommunications networks and acquired bandwidth are 3 to 20 years and 5 to 7 years for furniture fixtures, equipment and other. These useful lives are determined based on historical usage with consideration given to technological changes and trends in the industry that could impact the network architecture and asset utilization. This latter assessment is significant because we operate within an industry in which new technological changes could render some or all of our network related equipment obsolete requiring application of a shorter useful life or, in certain circumstances, a write-off of the entire value of the asset. Accordingly, in making this assessment, we consider our planned use of the assets, the views of experts both from internal and outside sources regarding the impact of technological advances and trends in the industry on the value and useful lives of our network assets. Costs of additions and improvements are capitalized and repairs and maintenance are charged to expense as incurred. Direct external and internal costs of constructing property and equipment are capitalized including interest costs related to construction. Depreciation or amortization of the long-lived assets, with finite lives, begins when the asset is substantially complete or placed into service.

Investments in broadband wireless licenses are amortized over the portion of the original license term remaining after the license is placed in service, or 10 years, whichever is shorter. The original license period is determined by the FCC. In order to receive an extension of the original license term from the FCC, we are required to show substantial service in the license area within ten years of being licensed. Failure to meet this requirement could result in forfeiture of the license. Approximately $23.5 million in book value of these licenses have not yet been placed into service. Had these licenses been in service during all of 2004, amortization expense would have increased by approximately $5.5 million. If we fail to show substantial service in the licensed geographic area at the end of the original ten year period and are not granted an extension or renewal from the FCC, we would forfeit the right to offer such services in that market. XO is evaluating recent improvements in the price and performance of broadband wireless equipment, and is developing a plan to meet the FCC's substantial service test in all its licensed areas before the licenses are due for renewal proceedings.

Other intangibles consist of customer relationships, internally developed technology and trade names. The customer relationships, internally developed technology and certain trade names are being amortized using the straight-line method over the estimated useful lives of three years. Certain trade names were determined to have indefinite lives and are not being amortized. Goodwill and indefinite life trade names are reviewed at least annually for impairment, as required under Statement of Financial Accounting Standards 142, "Goodwill and Other Intangible Assets", or SFAS No. 142. We retained independent appraisers to perform a preliminary valuation of our assets and liabilities as of December 31, 2004. This valuation was necessary as our estimated fair value as determined by our stock price, was less than our book value. Based on this appraisal we recorded a $212.5 million non-cash impairment charge on our goodwill. This report will be finalized in the first quarter of 2005 and could result in a change to this preliminary estimate.

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount should be addressed pursuant to SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," or SFAS No. 144. The criteria for determining impairment for long-lived assets to be held and used is determined by comparing the carrying value of these long-lived assets to management's best estimate of future undiscounted cash flows expected to result from the use of the assets and their eventual disposition. Based on our analysis, we believe that no impairment existed under SFAS No. 144 as of December 31, 2004. In the event that there are changes in the planned use of our long-lived assets or our expected future undiscounted cash flows are reduced significantly, our assessment of our ability to recover the carrying value of these assets under SFAS No. 144 could change.

Revenue Recognition

Revenues from telecommunications services are recognized when the services are performed, evidence of an arrangement exists, the charges are fixed and determinable and collectability is probable. In circumstances when these criteria are not met, revenue recognition is deferred until resolution occurs. For example, if a customer files for bankruptcy protection, we believe the probability of collection is weakened. Consequently, under such circumstances, although we continue to bill the customer for all services provided, we do not recognize revenue until cash is received. In addition, telecommunications customers often dispute the amounts that we invoice them due to regulatory issues, late payment fees, and early termination charges based on differences of opinion regarding contract terms or service levels. Accordingly, as these billings are not considered fixed and determinable and collection of such amounts is not considered probable while these amounts are disputed, revenue recognition is deferred until the dispute is resolved and the collection is probable.

Service discounts and incentives related to telecommunications services are recorded as a reduction of revenue when granted or ratably over a contract period. Fees billed in connection with customer installations and other non-recurring fees are deferred and recognized ratably over the estimated customer life of three years.

We establish an allowance for collection of doubtful accounts and other sales credit adjustments. Allowances for sales credits are established through a charge to revenue, while allowances for doubtful accounts are established through a charge to selling, operating and general expenses. We assess the adequacy of these reserves monthly by considering general factors, such as the length of time individual receivables are past due, historical collection experience, the economic and competitive environment, and changes in the creditworthiness of our customers. As considered necessary, we also assess the ability of specific customers to meet their financial obligations to us and establish specific valuation allowances based on the amount we expect to collect from these customers. We can and have experienced material changes to our reserve requirements on a month to month basis. We believe that our established credit and valuation allowances were adequate as of December 31, 2004. If circumstances relating to specific customers change or economic conditions worsen such that our past collection experience and assessment of the economic environment are no longer valid, our estimate of the recoverability of our trade receivables could be changed. If this occurs, we would adjust our valuation allowance in the period the new information is known.

Cost of Service

Cost of service includes expenses directly associated with providing telecommunications services to customers. We accrue for the estimated costs of services received from third party telecommunications providers during the period the services are received. Invoices received from the third party telecommunications providers are often disputed due to billing discrepancies. We accrue for all invoiced amounts, even amounts in dispute, as these amounts represent contingent liabilities that are considered probable and measurable. Disputes resolved in our favor may reduce cost of service in the period the dispute is settled. As the period of time required to resolve these types of disputes often lapses over several quarters, the benefits associated with the favorable resolution of such disputes are normally realized in periods subsequent to the accrual of the disputed amount.

Subsequent Events

On March 16, 2005, McLeodUSA Inc, McLeod, announced that it is looking into financial restructuring options due to its on-going cash requirements. XO currently holds McLeod debt securities that are included in marketable securities and other investments. It is too early to conclude what type of restructuring option McLeod will choose, or if any will be approved by their creditors and how that would impact our investment. Based on this announcement, there is a risk that the carrying value of $10.8 million will be impaired, and require adjustment in 2005.

Off-Balance Sheet Arrangements

We are not currently engaged in the use of off-balance sheet derivative financial instruments, to hedge or partially hedge interest rate exposure nor do we maintain any other off-balance sheet arrangements for the purpose of credit enhancement, hedging transactions, or other financial or investment purposes.

Recent Accounting Pronouncements Implemented in 2004

Statement No. 123 (revised 2004), "Share-Based Payment", SFAS 123R, was issued in December 2004. Once effective this statement will require entities to recognized compensation cost for all equity-classified awards granted, modified or settled after the effective date using the fair-value measurement method. In addition, public companies will recognize compensation expense for the unvested portion of awards outstanding as of the effective date based on their grant-date fair value as calculated under the original provisions of SFAS 123. The effective date for public entities is June 15, 2005. The amount of compensation expense that we record after the adoption of SFAS 123R in 2005 and beyond, will depend on the amount, timing and pricing of stock option grants.

Item 7A. Quantitative and Qualitative Disclosure About Market Risk

As of December 31, 2004, our Credit Facility was comprised of $361.0 million in secured loans and $5.2 million of accrued interest. Currently, we do not pay cash interest on the Credit Facility and accrued interest converts to principal ratably throughout the loan period. As interest accrues at variable rates, our Credit Facility subjects us to interest rate risks. Interest rate risk as of December 31, 2004 is illustrated in the following table (dollars in millions).

	Annual Interest Expense Given an Interest Rate decrease of X Basis Points			No Change in Interest Rates	Annual Interest Expense Given an Interest Rate increase of X Basis Points		
Interest Rate Risk	(150 BPS)	(100 BPS)	(50 BPS)	Fair Value	50 BPS	100 BPS	150 BPS
Credit Facility	$ 22.9	$ 24.8	$ 26.6	$ 28.4	$ 30.3	$ 32.1	$ 33.9

The sensitivity analysis provides only a limited, point in time view of the market risk sensitivity of the loans under our Credit Facility. The actual impact of market interest rate changes may differ significantly from those shown in the above sensitivity analysis.

Marketable securities, available for sale, at December 31, 2004 consist primarily of investments in equity and debt securities of publicly traded companies. The fair value of our investment in equity and debt securities exposes us to market risk. These investments are subject to changes in the market price of the securities. The table that follows summarizes the fair values of our marketable securities and provides a sensitivity analysis of the estimated fair value of these financial instruments assuming a 5%, 10% and 15% increase or decrease in market price (dollars in millions).

	Fair value assuming the following percentage decrease in market price			No Change in Fair Value	Fair value assuming the following percentage increase in market price		
Market Risk	15%	10%	5%	0%	5%	10%	15%
Market price	$ 14.0	$ 14.9	$ 15.7	$ 16.5	$ 17.4	$ 18.2	$ 19.0

Item 8. Financial Statements and Supplementary Data

Our consolidated financial statements are filed under this Item, beginning on page F-1 of this Report.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

On September 24, 2003, we notified our independent auditors, Ernst & Young LLP that our Audit Committee of our Board of Directors had decided to change auditors. On September 30, 2003, the Audit Committee of XO's Board of Directors appointed KPMG LLP to serve as its new independent registered public accounting firm for the year ending December 31, 2003. The change was effective immediately. Ernst & Young LLP's report on XO's consolidated financial statements as of and for the year ended December 31, 2002 did not contain an adverse opinion or disclaimer of opinion, nor was it qualified or modified as to uncertainty, audit scope or accounting principles. During the fiscal year ending December 31, 2002, there were: (i) no disagreements with Ernst & Young on any matter of accounting principle or practice, financial statement disclosure or auditing scope or procedure which, if not resolved to Ernst & Young's satisfaction, would have caused them to make reference to the subject matter in connection with their report on our financial statements for such years; and (ii) there were no reportable events as defined in Item 304(a)(1)(v) of Regulation S-K.

During the year ended December 31, 2002 and through the date of their appointment, we did not consult KPMG LLP with respect to the application of accounting principles to a specified transaction, either completed or proposed, or the type of audit opinion that might be rendered on our consolidated financial statements, or any other matters or reportable events listed in Items 304(a)(2)(i) and (ii) of Regulation S-K.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The term disclosure controls and procedures is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934. These rules refer to the controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within required time periods. Our Principal Executive Officer and our Principal Financial Officer have evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on the evaluation they have concluded that, as of the end of such period the controls and procedures were effective at ensuring that required information was disclosed on a timely basis in our report filed under the Exchange Act.

Changes in Internal Controls over Financial Reporting

We maintain a system of internal accounting controls that are designed to provide reasonable assurance that our books and records accurately reflect our transactions and that our established policies and procedures are followed. As of June 23, 2004, the newly combined company that includes the acquired Allegiance telecommunication assets has been aggressively working to consolidate overlapping processes, controls, and systems. With the exception of Carrier Access Billings and the legacy-Allegiance revenue cycle, the vast majority of overlapping processes, systems, and controls have migrated to the legacy-XO control environment. The Carrier Access Billings process for the combined entity has migrated to the legacy-Allegiance control environment. The legacy-Allegiance revenue and sales commission cycles remain unchanged but are subject to the same general internal controls over financial reporting that we apply to our legacy businesses, although they were excluded from our effectiveness evaluation as discussed below.

Management Report on Internal Control over Financial Reporting

Management of XO is responsible for establishing and maintaining adequate internal control over financial reporting as such term is defined in Exchange Act Rules 13a-15(f). In accordance with the

Securities and Exchange Commission Rulemaking Release Nos. 33-8238 and 34-47986 issued in August 2003, management has evaluated the effectiveness of XO's internal controls over financial reporting based on the framework in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission or more commonly referred to as the COSO Framework.

Based on our evaluation under the COSO framework, management has concluded that, XO's internal control over financial reporting was effective as of December 31, 2004. KPMG LLP, XO's independent registered public accounting firm, has audited the financial statements included in this Annual Report on Form 10-K, and has issued an attestation report on management's assessment of XO's internal control over financial reporting.

On June 23, 2004, XO completed the acquisition of all of the telecommunications services assets of Allegiance Telecom, Inc. (Allegiance), and management excluded from its assessment of the effectiveness of XO's internal control over financial reporting as of December 31, 2004, Allegiance's internal control over financial reporting associated with total revenues of approximately $217.2 million included in the consolidated financial statements of XO for the year ended December 31, 2004. Our exclusion of Allegiance's internal control over financial reporting is allowed by the Securities and Exchange Commission's response to Question No. 2 contained in the Frequently Asked Questions entitled *Management's Report on Internal Control Over Financial Reporting and Certification of Disclosure in Exchange Act Periodic Reports, Frequently Asked Questions (revised October 6, 2004).*

PART III

Item 10. Directors and Executive Officers of the Registrant

Certain information required by Items 401 and 405 of Regulation S-K is incorporated by reference from our definitive proxy statement for the 2005 Annual Meeting of Stockholders to be held on May 9, 2005 to be filed with the SEC pursuant to Regulation 14A within 120 days after the end of our 2004 fiscal year.

Audit Committee Financial Expert

Our Board of Directors has determined Robert Knauss is an "audit committee financial expert" as defined under Item 401(h) of Regulation S-K. Mr. Knauss is an independent director, as defined in Item 7(d)(3)(iv) of Schedule 14A.

Code of Ethics

We have adopted a Code of Ethics within the meaning of Item 406(b) of Regulation S-K. This Code of Ethics applies to our principal executive officer, our principal financial officer and principal accounting officer, as well as all other employees. This Code of Ethics is publicly available on our website at www.xo.com. If we make substantive amendments to this Code of Ethics or grant any waiver, including any implicit waiver, we will disclose the nature of such amendment or waiver on our website or in a report on Form 8-K within five days of such amendment or waiver.

Item 11. Executive Compensation

The information required by this Item is incorporated by reference from the information provided under the heading "Executive Compensation" of our Proxy Statement.

Item 12. Security Ownership of Certain Beneficial Owners and Management

Information required by this Item with respect to Securities Authorized for Issuance under Equity Compensation Plans is incorporated herein by reference from the information provided in the proposal to approve the amendment of our Directors' Stock Option Plan under the heading "Equity Compensation Plan" of our Proxy Statement.

Information required by this Item with respect to Stock Ownership of Certain Beneficial Owners and Management is incorporated herein by reference from the information provided under the heading "Stock Ownership of Certain Beneficial Owners and Management" of our Proxy Statement.

Item 13. Certain Relationships and Related Transactions

Various entities controlled by Mr. Icahn hold the following interests in XO:

	Outstanding Common Stock	Warrants	Credit Facility	Preferred Stock Outstanding
At December 31, 2004	Greater than 50%	Greater than 40%	Greater than 90%	95%

The terms of the common stock, warrants and the Credit Facility, as well as the lease and tax allocation agreements discussed below, were all approved by the bankruptcy court as part of the Chapter 11 proceedings from which XO emerged in January 2003.

In August 2004, after the closing of the Preferred Stock Offering discussed in Part II, Item 7, Mr. Icahn filed a schedule 13D amendment with the Securities and Exchange Commission disclosing that his beneficial ownership, as defined therein, was 60.7% of XO.

As a result of his significant majority ownership, Mr. Icahn has the right to elect all of XO's directors, who in turn have the right to (i) appoint the members of the committees of XO's Board of Directors, (ii) appoint key members of XO's executive management team, and (iii) appoint XO's auditors. Currently, Mr. Icahn is Chairman of the Board of Directors and three employees of Icahn Associates also sit on the Board of Directors and various committees of the Board of Directors. Under applicable law and XO's Certificate of Incorporation and by-laws, certain actions cannot be taken without the approval of holders of a majority of the Company's voting stock, including, without limitation, mergers, acquisitions, the sale of substantially all of the assets, and amendments to XO's Certificate of Incorporation and by-laws.

Mr. Icahn, through various entities that he owns or controls, has the right to require XO to register, under the Securities Act of 1933, shares of XO's Common Stock held by such entities and to include shares of XO's Common Stock held by them in certain registration statements filed by XO.

Dixon Properties, LLC or Dixon, which is controlled by Mr. Icahn, owns the building in which XO's headquarters is located. XO currently leases approximately 170,000 square feet of space in that building. Pursuant to the lease agreement, XO has paid $3.5 million in lease rent to Dixon for the year ended December 31, 2004, and XO is obligated to pay approximately $12.1 million to Dixon through the expiration of the initial term of the lease, which is November 30, 2007.

XO entered into a Tax Allocation Agreement, dated January 16, 2003, between XO and Starfire Holding Corporation or Starfire, the parent entity of the affiliated group of corporations controlled by Mr. Icahn. XO and Starfire filed consolidated returns during the period in which Mr. Icahn's ownership of XO was equal to or greater than 80%, as required by the Internal Revenue Code. Upon the closing of the Rights Offering in January 2004, Mr. Icahn's ownership percentage fell below 80%. Consequently, XO is no longer included as part of Starfire's consolidated group after January 2004. Upon deconsolidation, the Tax Allocation Agreement generally provides that Starfire will reimburse XO each year going forward for the excess of XO's actual income tax expense over the income tax that XO would have owed if the net operating losses or other tax attributes used in prior periods by the Starfire consolidated group were still available to XO.

The Company provides certain telecommunications services to companies affiliated with Mr. Icahn. For the year ended December 31, 2004, the total revenue recognized on such services to Icahn Affiliates was approximately $2.0 million. During the year ended December 31, 2004, the Company purchased approximately $0.6 million in services from Icahn Affiliates. During the year ended December 31, 2004, the Company purchased $1.0 million in hardware and services from Dell, Inc. Mr. Adam Dell, an XO director, is the brother of Mr. Michael Dell, the Chairman of Dell, Inc.

XO provided telecommunications services to Allegiance from February 18, 2004 through the Closing Date. Total revenue recognized for those services was approximately $1.7 million. In addition, XO provided Allegiance management services under an Operating Agreement between the Early Funding Date of April 13, 2004 and the Closing Date. XO believes it is owed a monies under the terms of the Operating Agreement and this is part of the total claim that is discussed in Part I, Item 3. Based on the contingent nature of this claim, it is not recorded in the accompanying consolidated financial statements.

On June 8, 2004 XO entered into a Registration Rights Agreement with the ATLT, holder of approximately 24.9% of XO's outstanding common stock, pursuant to which XO agreed to utilize its best efforts to register for public resale, the 45,380,000 shares of XO common stock issued as part of the acquisition of the Acquired Businesses. XO has not filed such registration statement.

On November 2, 2004, XO entered into an Indemnification Agreement with each of Mrs. Dell, Knauss and Gradin, each of whom is an independent member of XO's Board of Directors, pursuant to which XO has agreed to indemnify each of such directors for any personal liability and costs that he may incur in connection with the performance of services as a director of XO, and advance to each such director any expenses that he may incur in connection with any litigation or actions related to such services.

Item 14. Principal Accounting Fees and Services

Information with respect to fees paid to our principal accountant and our audit committee's pre-approval policies and procedures are incorporated herein by reference to the Proxy Statement to be filed pursuant to Regulation 14A.

PART IV

Item 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

(a) (1) and (2) Financial Statements and Schedule:

(3) List of Exhibits — Refer to Exhibit Index, which is incorporated herein by reference.

SIGNATURES

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

XO Communications, Inc.

Date: March 18, 2005

By: /s/ CARL J. GRIVNER

Carl J. Grivner
President and Chief Executive Officer
(Principal Executive Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on or before March , 2004 by the following persons on behalf of the Registrant and in the capacities indicated:

Name	Title
/s/ CARL J. GRIVNER Carl J. Grivner	President and Chief Executive Officer, Director (Principal Executive Officer)
/s/ WILLIAM GARRAHAN William Garrahan	Senior Vice President and Acting Chief Financial Officer (Principal Financial Officer)
/s/ CARL C. ICAHN Carl C. Icahn	Chairman of the Board of Directors
/s/ ANDREW R. COHEN Andrew R. Cohen	Director
/s/ ADAM DELL Adam Dell	Director
/s/ FREDRIK GRADIN Fredrik Gradin	Director
/s/ VINCENT J. INTRIERI Vincent J. Intrieri	Director
/s/ ROBERT L. KNAUSS Robert L. Knauss	Director
/s/ KEITH MEISTER Keith Meister	Director

EXHIBIT INDEX

2.1	Third Amended Plan of Reorganization of XO Communications, Inc., dated July 22, 2002, (Incorporated herein by reference to exhibit 2.1 filed with the Current Report on Form 8-K/ A of XO Communications, Inc., filed on November 26, 2002).
2.2	Plan Supplement, dated October 23, 2003, to the Third Amended Plan of Reorganization of XO Communications, Inc., dated July 22, 2002 (Incorporated herein by reference to exhibit 2.2 filed with the Current Report on Form 8-K/ A of XO Communications, Inc., filed on November 26, 2002).
2.3	Order Confirming Third Amended Plan of Reorganization, dated November 15, 2002 (Incorporated herein by reference to exhibit 99.1 filed with the Current Report on Form 8-K/ A of XO Communications, Inc., filed on November 26, 2002).
2.4	Asset Purchase Agreement, dated as of February 18, 2004, by and among XO Communications, Inc., Allegiance Telecom, Inc., and Allegiance Telecom Company Worldwide (Incorporated herein by reference to exhibit 10.1 filed with the Current Report on Form 8-K of XO Communications, Inc. filed on February 24, 2004).
3.1	Amended and Restated Certificate of Incorporation of XO Communications, Inc. (Incorporated herein by reference to exhibit 3.1 filed with the Registration Statement on Form 8-A of XO Communications, Inc., filed on February 7, 2003, pursuant to the Securities Exchange Act).
3.2	Certificate of Designations setting forth the powers, preferences and relative, participating, optional and other special rights of the 6% Class A Convertible Preferred Stock (Incorporated by reference herein to exhibit 3.1 filed with the Quarterly Report on Form 10-Q of XO Communications, Inc. filed on August 9, 2004).
3.3	Amended and Restated Bylaws of XO Communications, Inc. (Incorporated by reference herein to exhibit 3.1 filed with the Annual Report on Form 10-K of XO Communications, Inc. filed on March 15, 2004).
4.1	Form of Stock Certificate of Common Stock (Incorporated herein by reference to exhibit 4.1 filed with the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003.)
4.2	Series A Warrant Agreement, dated as of January 16, 2003, by and between XO Communications, Inc. and American Stock Transfer & Trust Company (Incorporated herein by reference to exhibit 10.1 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).
4.3	Series B Warrant Agreement, dated as of January 16, 2003, by and between XO Communications, Inc. and American Stock Transfer & Trust Company (Incorporated herein by reference to exhibit 10.2 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).
4.4	Series C Warrant Agreement, dated as of January 16, 2003, by and between XO Communications, Inc. and American Stock Transfer & Trust Company (Incorporated herein by reference to exhibit 10.3 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).
10.1	XO Communications, Inc. 2002 Stock Incentive Plan (Incorporated herein by reference to exhibit 10.1.1 to the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003).
10.2	XO Communications, Inc. Retention Bonus and Incentive Plan (Incorporated herein by reference to exhibit 10.1.2 to the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003).
10.3	Registration Rights Agreement, dated as of January 16, 2003, between XO Communications, Inc. and High River Limited Partnership and Meadow Walk Limited Partnership (Incorporated herein by reference to exhibit 10.4 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).

10.4	Registration Rights Agreement, dated as of August 6, 2004, by and among XO Communications, Inc., Tramore LLC, Cardiff Holdings, LLC and Amalgamated Gadget, L.P. (Incorporated herein by reference to exhibit 10.1 filed with the Quarterly Report on Form 10-Q filed by XO Communications, Inc. for the quarterly period ended June 30, 2004, filed on August 9, 2004).
10.5	Registration Rights Agreement, dated as of June 23, 2004, by and among Allegiance Telecom, Inc., Allegiance Telecom Company Worldwide, the Allegiance Telecom Liquidating Trust, and XO Communications, Inc.
10.6	Tax Allocation Agreement, dated as of January 16, 2003, between XO Communications, Inc. and Starfire Holding Corporation (Incorporated herein by reference to exhibit 10.5 filed with the Current Report on Form 8-K of XO Communications, Inc., filed on January 30, 2003).
10.7	Employment Term Sheet, dated as of April 30, 2003, delivered by XO Communications, Inc. to Carl J. Grivner, President and Chief Executive Officer of XO Communications, Inc. (Incorporated herein by reference to exhibit 10.1 filed with the Quarterly Report on Form 10-Q of XO Communications, Inc. for the three months ended March 31, 2003, filed on May 15, 2003).
10.8	Change in Control Agreement by and between XO Communications, Inc. and Carl J. Grivner, President and Chief Executive Officer of XO Communications, Inc. (Incorporated herein by reference to exhibit 10.2 filed with the Quarterly Report on Form 10-Q of XO Communications, Inc. for the three months ended March 31, 2003, filed on May 15, 2003).
10.9	Employment Agreement, effective as of September 25, 2000, by and between Wayne M. Rehberger and XO Communications, Inc. (Incorporated by reference herein to exhibit 10.10 filed with the Annual Report on Form 10-K of XO Communications, Inc. filed on March 15, 2004).
10.10	Indemnification Agreement by and between Robert Knauss and XO Communications, Inc., dated as of November 2, 2004. (Incorporated herein by reference to exhibit 10.2 filed with the Quarterly Report on Form 10-Q filed by XO Communications, Inc. for the quarterly period ended September 30, 2004, filed on November 9, 2004).
10.11	Indemnification Agreement by and between Adam Dell and XO Communications, Inc., dated as of November 2, 2004. (Incorporated herein by reference to exhibit 10.1 filed with the Quarterly Report on Form 10-Q filed by XO Communications, Inc. for the quarterly period ended September 30, 2004, filed on November 9, 2004).
10.12	Indemnification Agreement by and between Fredrik Gradin and XO Communications, Inc., dated as of November 2, 2004. (Incorporated herein by reference to exhibit 10.3 filed with the Quarterly Report on Form 10-Q filed by XO Communications, Inc. for the quarterly period ended September 30, 2004, filed on November 9, 2004).
10.13	Cost Sharing and IRU Agreement, dated July 18, 1998, between Level 3 Communications, LLC and XO Intercity Holdings No. 2, LLC (f/k/a INTERNEXT LLC) (Incorporated herein by reference to exhibit 10.8 filed with the quarterly report on Form 10-Q for the quarterly period ended September 30, 1998 of NEXTLINK Communications, Inc. and NEXTLINK Capital, Inc., filed on November 16, 1998).
10.14	Master Agreement, dated August 8, 2002, between Level 3 Communications, Inc. and XO Communications, Inc. (Incorporated herein by reference to exhibit 10.4.2 filed with the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003).
10.15	Amended and Restated Credit and Guaranty Agreement, dated as of January 16, 2003, among XO Communications, Inc., certain subsidiaries of XO Communications, Inc., the Lenders party thereto from time to time, and Mizuho Corporate Bank, as Administrative Agent (Incorporated herein by reference to exhibit 10.5 filed with the Annual Report on Form 10-K of XO Communications, Inc. for the year ended December 31, 2002, filed on March 21, 2003).
10.16	XO Communications, Inc. Code of Ethics (Incorporated by reference herein to exhibit 14.1 filed with the Annual Report on Form 10-K of XO Communications, Inc. filed on March 15, 2004).
21.1	Subsidiaries of XO Communications, Inc.
23.1	Consent of KPMG LLP

23.2	Consent of Ernst & Young LLP
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act, as amended.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
XO Communications, Inc.:

We have audited management's assessment, included in the accompanying Management Report on Internal Control over Financial Reporting that XO Communications, Inc. and subsidiaries (XO) maintained effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). XO's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that XO maintained effective internal control over financial reporting as of December 31, 2004, is fairly stated, in all material respects, based on criteria established in Internal Control -Integrated Framework issued by COSO. Also, in our opinion, XO maintained, in all material respects, effective internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control -Integrated Framework issued by COSO.

On June 23, 2004, XO completed the acquisition of all of the telecommunications services assets of Allegiance Telecom, Inc. (Allegiance), and management excluded from its assessment of the effectiveness of XO's internal control over financial reporting as of December 31, 2004, Allegiance's internal control over financial reporting associated with total revenues of approximately $217.2 million included in the consolidated financial statements of XO for the year ended December 31, 2004. Our audit of internal control over financial reporting of XO also excluded an evaluation of Allegiance's internal control over financial reporting.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of XO as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity and cash flows for the year ended December 31, 2004 and the period from January 1, 2003 to December 31, 2003, and for the portion of January 1, 2003, related to Predecessor XO's reorganization gain and our report dated March 18, 2005 expressed an unqualified opinion on those consolidated financial statements and the related 2004 and 2003 consolidated financial statement schedule.

/s/ KPMG LLP
McLean, Virginia

March 18, 2005

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders
XO Communications, Inc.:

We have audited the accompanying consolidated balance sheets of XO Communications, Inc. and subsidiaries (XO) as of December 31, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity, and cash flows for the year ended December 31, 2004 and for the period from January 1, 2003 to December 31, 2003 (XO period) and for the portion of January 1, 2003, related to Predecessor XO's reorganization gain (Predecessor XO period). In connection with our audits of the XO period, we have also audited the 2004 and 2003 consolidated financial statement schedule as listed in the accompanying index. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). 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 XO period consolidated financial statements referred to above present fairly, in all material respects, the financial position of XO Communications, Inc. and subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for the XO period, in conformity with U.S. generally accepted accounting principles. Further, in our opinion, the Predecessor XO period consolidated financial statements referred to above present fairly, in all material respects, the results of their operations and their cash flows for the portion of January 1, 2003 related to the Predecessor's reorganization gain in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related 2004 and 2003 consolidated financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, present fairly, in all material respects, the information set forth therein.

As discussed in Note 20 to the consolidated financial statements, on January 16, 2003, XO Communications, Inc. emerged from bankruptcy. The consolidated financial statements of XO reflect the impacts of adjustments to reflect the fair value of assets and liabilities under fresh start reporting, which was applied effective January 1, 2003. As a result, the consolidated financial statements of XO are presented on a different basis than those of Predecessor XO and, therefore, are not comparable in all respects.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of XO's internal control over financial reporting as of December 31, 2004, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 18, 2005 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting. On June 23, 2004, XO completed the acquisition of all of the telecommunications services assets of Allegiance Telecom, Inc. (Allegiance), and management excluded from its assessment of the effectiveness of XO's internal control over financial reporting as of December 31, 2004, Allegiance's internal control over financial reporting associated with total revenues of approximately $217.2 million included in the consolidated financial statements of XO for the year ended December 31, 2004. Our audit of internal control over financial reporting of XO also excluded an evaluation of Allegiance's internal control over financial reporting.

/s/ KPMG LLP

March 18, 2005

McLean, VA

REPORT OF ERNST & YOUNG LLP,

INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We have audited the accompanying consolidated statements of operations, stockholders' equity (deficit) and cash flows of XO Communications, Inc. (the "Company") for the year ended December 31, 2002. Our audit also included the financial statement schedule listed in the Index at item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audit.

We conducted our audit in accordance with the standards of the Public Accounting Oversight Board (United States). 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 audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated results of operations and cash flows of XO Communications, Inc. for the year ended December 31, 2002, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

As discussed in Note 2 to the consolidated financial statements, effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets".

As discussed in Note 20 to the consolidated financial statements, effective January 16, 2003, the Company was reorganized under a plan of reorganization confirmed by the United States Bankruptcy Court for the Southern District of New York. In connection with its reorganization, the Company will apply fresh start accounting in the first quarter of 2003.

/s/ ERNST & YOUNG LLP

Baltimore, Maryland
February 28, 2003

XO Communications, Inc.

Consolidated Balance Sheets
(Dollars in thousands, except for share and per share data)

	December 31, 2004	December 31, 2003
ASSETS		
Current assets:		
Cash and cash equivalents	$ 233,989	$ 478,560
Marketable securities and other investments	17,300	42,052
Accounts receivable, net of allowance for doubtful accounts of $38,981 and $32,986, at December 31, 2004 and 2003, respectively	150,101	93,958
Other current assets	50,864	12,421
Total current assets	452,254	626,991
Property and equipment, net	820,536	485,984
Broadband wireless licenses and other intangibles, net	139,866	109,515
Other assets	46,729	42,675
Total assets	$ 1,459,385	$ 1,265,165
LIABILITIES, CONVERTIBLE PREFERRED STOCK AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 88,010	$ 63,064
Accrued liabilities	241,532	208,353
Total current liabilities	329,542	271,417
Long-term debt and accrued interest payable	366,247	536,791
Other long-term liabilities	73,691	76,532
Total liabilities	769,480	884,740
Class A convertible preferred stock	204,353	—
Commitments and contingencies		
Stockholders' equity:		
Preferred stock: par value $0.01 per share, 200,000,000 shares authorized: 4,000,000 shares of Class A convertible preferred stock issued and outstanding on December 31 2004	—	—
Warrants and common stock, par value $0.01 per share, 1,000,000,000 shares authorized: 181,933,035 and 96,274,140 shares issued and outstanding on December 31 2004 and December 31, 2003, respectively	989,511	482,440
Subscription rights exercised, 32,503,234 shares authorized: none issued and outstanding	—	162,516
Subscription rights receivable, 32,503,234 shares authorized: none issued and outstanding	—	(162,516)
Deferred compensation	(574)	(839)
Accumulated other comprehensive income	4,712	1,378
Accumulated deficit	(508,097)	(102,554)
Total stockholders' equity	485,552	380,425
Total liabilities, convertible preferred stock and stockholders' equity	$ 1,459,385	$ 1,265,165

See accompanying notes to the consolidated financial statements.

XO Communications, Inc.

Consolidated Statements of Operations
(Dollars in thousands, except for share and per share data)

	Year Ended December 31, 2004	Year Ended December 31, 2003	Predecessor XO January 1, 2003	Predecessor XO Year Ended December 31, 2002
Revenue	$ 1,300,420	$ 1,110,483	$ —	$ 1,259,853
Costs and expenses:				
Cost of service (excludes depreciation and amortization)	552,735	422,129	—	522,924
Selling, operating and general	727,666	679,286	—	765,853
Depreciation and amortization	177,781	109,308	—	699,806
Goodwill impairment charge	212,530	—	—	—
Restructuring and asset write-downs	—	11,618	—	480,168
Total costs and expenses	1,670,712	1,222,341	—	2,468,751
Loss from operations	(370,292)	(111,858)	—	(1,208,898)
Investment (loss) income, net	(9,037)	46,152	—	16,278
Interest expense, net	(26,214)	(36,848)	—	(226,451)
Reorganization gain (expense), net	—	—	3,032,282	(91,121)
Net (loss) income before cumulative effect of accounting change	(405,543)	(102,554)	3,032,282	(1,510,192)
Cumulative effect of accounting change	—	—	—	(1,876,626)
Net (loss) income	(405,543)	(102,554)	3,032,282	(3,386,818)
Recognition of preferred stock modification fee, net — reorganization item	—	—	—	78,703
Preferred stock dividends and accretion of preferred stock redemption obligation, net	(4,910)	—	—	(42,247)
Net (loss) income applicable to common shares	$ (410,453)	$ (102,554)	$ 3,032,282	$ (3,350,362)
Net (loss) income per common share, basic and diluted:				
Net (loss) income before cumulative effect of accounting change	$ (2.54)	$ (1.07)	$ 6.86	$ (3.42)
Cumulative effect of accounting change	—	—	—	(4.24)
Net (loss) income	(2.54)	(1.07)	6.86	(7.66)
Recognition of preferred stock modification fee, net — reorganization item	—	—	—	0.18
Preferred stock dividends and accretion of preferred stock redemption obligation, net	(0.03)	—	—	(0.10)
Net (loss) income per common share, basic and diluted	$ (2.57)	$ (1.07)	$ 6.86	$ (7.58)
Weighted average shares, basic and diluted	159,883,403	95,632,859	441,964,342	441,964,342

See accompanying notes to consolidated financial statements.

XO Communications, Inc.

Consolidated Statements of Stockholders' Equity
(Dollars in thousands, except share data)

	Common Stock		Subscription Rights Exercised		Subscription Receivable					
	Shares	Amount	Shares	Amount	Shares	Amount	Deferred Compensation	Accumulated Deficit	Accumulated Other Comprehensive Income	Total
Balance at January 1, 2003	—	$ —	—	$ —	—	$ —	$ —	$ —	$ —	$ —
Issuance of common stock	95,000,001	475,000	32,503,234	162,516	(32,503,234)	(162,516)	—	—	—	475,000
Issuance of common stock through employee benefit plans, net	1,274,139	7,440	—	—	—	—	(839)	—	—	6,601
Comprehensive loss:										
Net loss	—	—	—	—	—	—	—	(102,554)	—	(102,554)
Other comprehensive income — unrealized holding gains arising during the year	—	—	—	—	—	—	—	—	1,378	1,378
Total comprehensive loss	—	—	—	—	—	—	—	—	—	(101,176)
Balance at December 31, 2003.	96,274,140	482,440	32,503,234	162,516	(32,503,234)	(162,516)	(839)	(102,554)	1,378	380,425
Issuance of common stock for acquisition	45,380,000	311,306	—	—	—	—	—	—	—	311,306
Issuance of common stock under rights offering	39,722,466	197,612	(32,503,234)	(162,516)	32,503,234	162,516	—	—	—	197,612
Issuance of common stock through employee benefit plans, net	556,429	3,063	—	—	—	—	265	—	—	3,328
Preferred stock accretion	—	(4,910)	—	—	—	—	—	—	—	(4,910)
Comprehensive loss:										
Net loss	—	—	—	—	—	—	—	(405,543)	—	(405,543)
Other comprehensive income — unrealized holding gains arising during the year, net	—	—	—	—	—	—	—	—	3,334	3,334
Total comprehensive loss	—	—	—	—	—	—	—	—	—	(402,209)
Balance at December 31, 2004	181,933,035	$989,511	—	$ —	—	$ —	$ (574)	$ (508,097)	$ 4,712	$ 485,552

See accompanying notes to consolidated financial statements.

XO Communications, Inc.

Consolidated Statements of Stockholders' Equity (Deficit)
(Dollars in thousands, except share data)

Predecessor Company	Common Stock Shares Class A	Common Stock Shares Class B	Common Stock Amount	Deferred Compensation	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Total
Balance at December 31, 2001	337,774,204	104,423,158	$ 4,628,509	$ (37,428)	$ 10,406	$ (4,304,071)	$ 297,416
Compensation attributable to stock options and restricted stock vesting	—	—	—	28,928	—	—	28,928
Issuance of common stock through employee benefit plans	85,854	—	24	—	—	—	24
Conversion of 6¹/₂% redeemable cumulative preferred stock into Class A common stock	3,173	—	35	—	—	—	35
Conversion of Preferred Stock	23,570	—	—	—	—	—	—
Refund of Employee Stock Purchase Plan funds withheld after cancellation(a)		—	(429)	—	—	—	(429)
Cancellation of Craig McCaw's Class A common stock	(6,853,582)	—	—	—	—	—	—
Comprehensive loss:							
Net loss	—	—	—	—	—	(3,386,818)	(3,386,818)
Recognition of preferred stock modification fee, net — reorganization item	—	—	—	—	—	78,703	78,703
Preferred stock dividends and accretion of preferred stock redemption obligation, net	—	—	—	—	—	(42,247)	(42,247)
Realized net losses and foreign currency translation adjustments transferred to current period earnings	—	—	—	—	(7,894)	—	(7,894)
Total comprehensive loss	—	—	—	—	—	—	(3,358,256)
Balance at December 31, 2002	331,033,219	104,423,158	4,628,139	(8,500)	2,512	(7,654,433)	(3,032,282)
Cancellation of predecessor common sock, deferred compensation, accumulated deficit and accumulated other comprehensive income under Plan of Reorganization	(331,033,219)	(104,423,158)	(4,628,139)	8,500	(2,512)	7,654,433	3,032,282
Balance at January 1, 2003.	—	—	$ —	$ —	$ —	$ —	$ —

(a) In the latter half of 2001, the Company's Employee Stock Purchase Plan was cancelled; however employee salary deferrals continued in December 2001, and were subsequently refunded in early 2002.

See accompanying notes to consolidated financial statements.

XO Communications, Inc.

Consolidated Statements of Cash Flows
(Dollars in thousands)

	Year Ended December 31, 2004	Year Ended December 31, 2003	Predecessor XO January 1, 2003	Predecessor XO Year Ended December 31, 2002
OPERATING ACTIVITIES:				
Net (loss) income	$ (405,543)	$ (102,554)	$ 3,032,282	$ (3,386,818)
Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities:				
Goodwill impairment charge	212,530	—	—	—
Depreciation and amortization	177,781	109,308	—	699,806
Accrual of interest	27,068	36,791	—	—
Stock-based compensation	406	708	—	28,928
Realized loss (gain) on investments	5,238	(27,224)	—	—
Non-cash restructuring charges and asset write-downs	10,360	6,765	—	477,250
Non-cash reorganization (gain) expense, net	—	—	(3,032,282)	89,448
Cumulative effect of accounting change	—	—	—	1,876,626
Changes in assets and liabilities, net of effects from acquisitions:				
Accounts receivable	(8,084)	22,583	—	85,514
Other assets	(9,952)	1,317	—	(21,572)
Accounts payable	8,503	(7,568)	—	—
Accrued liabilities	(18,157)	(33,825)	—	—
Other liabilities subject to compromise	—	—	—	195,904
Other liabilities not subject to compromise	—	—	—	(27,484)
Net cash provided by (used in) operating activities	150	6,301	—	17,602
INVESTING ACTIVITIES:				
Capital expenditures, net	(106,023)	(82,346)	—	(208,713)
Sales of marketable securities and investments	22,848	473,423	—	367,230
Purchases of marketable securities and investments	(36,413)	(238,041)	—	(103,935)
Cash (paid for) received from (acquisitions) divestitures	(325,249)	—	—	3,000
Net cash (used in) provided by investing activities	(444,837)	153,036	—	57,582
FINANCING ACTIVITIES:				
Proceeds from issuance of common stock, net	200,326	6,452	—	—
Proceeds from issuance of preferred stock, net	199,443	—	—	—
Repayments of long term debt and capital leases	(199,653)	(1,267)	—	(6,079)
Net cash provided by (used in) financing activities	200,116	5,185	—	(6,079)
Effect of exchange rate changes on cash	—	—	—	(1,256)
Net (decrease) increase in cash and cash equivalents	(244,571)	164,522	—	67,849
Cash and cash equivalents, beginning of year	478,560	314,038	314,038	246,189
Cash and cash equivalents, end of year	$ 233,989	$ 478,560	$ 314,038	$ 314,038

See accompanying notes to consolidated financial statements.

XO Communications, Inc.

Notes to Consolidated Financial Statements
December 31, 2004, 2003 and 2002

1. ORGANIZATION AND DESCRIPTION OF BUSINESS

Overview

XO Communications Inc., a Delaware corporation, through its subsidiaries, owns and operates an integrated metropolitan and nationwide fiber optic network that provides a comprehensive array of telecommunication services to business customers in over 70 United States markets. Voice services include local and long distance services, calling card and interactive voice response systems. Data services include Internet access, private data networking and hosting services. XO, through its subsidiaries, also offers integrated combined voice and data services in flat rate "bundled" packages. The consolidated financial statements include the accounts and activities of XO, and its subsidiaries (collectively referred to as the "Company" or "XO"). On June 23, 2004, XO completed the acquisition of all of the telecommunications services assets of Allegiance Telecom, Inc. The accompanying financial statements include the results of operations from this acquisition from June 23, 2004 through December 31, 2004. See note 2 for additional information.

2. BUSINESS COMBINATIONS

On June 23, 2004 (the "Closing Date"), XO completed the acquisition of all of the telecommunications services assets (the "Acquired Businesses") of Allegiance Telecom, Inc. ("ATI") under the terms of the Asset Purchase Agreement (the "Purchase Agreement") entered into on February 18, 2004 by and among the Company, ATI and Allegiance Telecom Company Worldwide (together with ATI, "Allegiance"), and approved by the United States Bankruptcy Court for the Southern District of New York (the "Bankruptcy Court") on February 19, 2004. Allegiance and its direct and indirect subsidiaries operated as debtors-in-possession under the Bankruptcy Code from May 14, 2003 to June 23, 2004. Allegiance was a facilities-based national local exchange carrier that provided integrated telecommunications services to business and other institutional customers in 36 major metropolitan areas across the United States. Allegiance's service offerings included voice, data, and integrated telecommunications services. XO did not acquire Allegiance's customer premises installation and maintenance business, shared hosting business, or dedicated dial-up Internet access service business (the "Unacquired Businesses").

Under the Purchase Agreement, XO paid approximately $636.6 million for the Acquired Businesses consisting of approximately $325.2 million of cash, including $14.1 million of adjustments for working capital and direct costs, and 45,380,000 shares of XO common stock valued at approximately $311.3 million using XO's common stock market price for a reasonable period before and after the Allegiance acquisition was announced.

After the Closing Date, the Unacquired Businesses as well as the ongoing Allegiance bankruptcy claims were transferred from Allegiance to the Allegiance Telecom Liquidating Trust (the "ATLT"). XO filed an administrative claim with the Bankruptcy Court in August 2004 against the ATLT, for at least approximately $40.0 million under the Purchase Agreement and other agreements between the parties. Subsequently, XO informed the ATLT that the amount in dispute approximates $50.0 million. The ATLT has counter claimed in correspondence that it believes it is owed approximately $100 million in respect to operating, working capital and other disputes that have arisen between the parties. XO is vigorously pursuing its claim and believes that the ATLT's counter claim is frivolous and completely without merit. XO and the ATLT are litigating their case, and are in the early stages of the litigation. The accompanying financial statements do not include any financial impact from this litigation as it is too early in the process to assess any outcome.

Upon the Closing Date, XO acquired title to the Acquired Businesses. XO retained independent appraisers to determine the fair value of the property, plant and equipment and intangible assets acquired as required under SFAS 141 "Business Combinations", ("SFAS No 141"). The following are the estimated fair value of assets acquired and liabilities assumed as of the Closing Date (dollars in thousands):

Current assets	$ 51,618
Property and equipment	372,405
Goodwill	212,530
Other intangible assets	68,052
Other long-term assets	2,933
Total assets acquired	707,538
Current liabilities	(58,193)
Long-term liabilities	(12,790)
Total liabilities acquired	(70,983)
Purchase price	$ 636,555

Of the $68.1 million of acquired intangible assets, approximately $5.7 million was assigned to various trade names and are being amortized over four years and approximately $62.4 million was assigned to the Acquired Businesses' customer base, which has an estimated useful life of 3 years. The values assigned in these financial statements are preliminary and represent management's best estimate of current values which are subject to revision due to changes in estimates of fair value as well as the pending claim discussed above. The goodwill recorded from this acquisition was adjusted for impairment as discussed in note 3.

The results of operations for the Acquired Businesses are included in the accompanying consolidated financial statements from the Closing Date through December 31, 2004. The following is unaudited pro forma financial information of the Company assuming the Allegiance acquisition had occurred at the beginning of the periods presented (dollars in thousands, except share and per share data):

	Year Ended December 31, 2004	Year Ended December 31, 2003
Revenue	$ 1,529,753	$ 1,630,042
Net loss applicable to common shares	$ (471,690)	$ (336,580)
Net loss per common share — basic and diluted	$ (2.60)	$ (2.39)
Weighted average shares — basic and diluted	181,457,087	141,012,858

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Principles of Consolidation

The Company's consolidated financial statements include all of the assets, liabilities and results of operations of subsidiaries in which the Company has a controlling interest. All inter-company accounts and transactions among consolidated entities have been eliminated.

(b) Use of Estimates and Assumptions

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Management periodically assesses the accuracy of these estimates and assumptions. Actual results could differ from those estimates.

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

(c) 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. Cash equivalents consist primarily of money market accounts that are available on demand. The carrying amount of these instruments approximates fair value due to their short maturities.

(d) Marketable Securities and Other Investments

The Company's marketable securities currently consist of debt and equity investments in publicly traded companies. The Company classifies its investments in equity securities as available-for-sale and records such investments at fair value. The fair values are based on quoted market prices. Other investments are recorded at cost, which approximates fair value. Unrealized gains and losses on available-for-sale marketable securities are reported as a separate component of comprehensive income. Realized gains and losses for available-for-sale securities are recognized in investment income.

(e) Long-Lived Assets

Long-lived assets include property and equipment, broadband wireless licenses, and intangible assets to be held and used. Long-lived assets, excluding intangible assets with indefinite useful lives, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount should be addressed pursuant to SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," ("SFAS No. 144"). The criteria for determining impairment for such long-lived assets to be held and used is determined by comparing the carrying value of these long-lived assets to management's best estimate of future undiscounted cash flows expected to result from the use of the assets. The Company believes that no impairment existed under SFAS No. 144 as of December 31, 2004. In the event that there are changes in the planned use of the Company's long-lived assets or its expected future undiscounted cash flows are reduced significantly, the Company's assessment of its ability to recover the carrying value of these assets under SFAS No. 144 could change.

Intangible assets with indefinite useful lives are tested for impairment annually during the fourth quarter, or more frequently if an event indicates that the asset might be impaired, in accordance with SFAS No. 142, "Goodwill and Other Intangible Assets" ("SFAS No. 142"). XO retained independent appraisers to perform a preliminary valuation of its assets and liabilities as of December 31, 2004. This valuation was necessary as XO's fair value as determined by its stock price, was less than its book value. Based on this appraisal, XO recorded a $212.5 million non-cash impairment charge on its goodwill. This report will be finalized in the first quarter of 2005, and could result in a change to this preliminary estimate. The Company performed the required transitional impairment tests of goodwill primarily from the Concentric merger as of January 1, 2002, and determined that the goodwill was totally impaired. Accordingly, in the first quarter of 2002 the Company recognized a $1,876.6 million charge as a cumulative effect of accounting change to write off all of its goodwill.

(f) Property and Equipment

Additions to property and equipment during 2004 and 2003 are stated at cost. Property and equipment acquired prior to December 31, 2002 is stated at its fair value at January 1, 2003. Depreciation is calculated on a straight-line basis over the estimated useful lives of the assets beginning in the month telecommunications networks and acquired bandwidth are substantially complete and available for use and in the month equipment and furniture are acquired. Telecommunications networks and bandwidth include the deployment of fiber optic cable and telecommunications hardware and software for the expressed purpose of delivering telecommunications services. Costs of additions and improvements are capitalized, and repairs and maintenance are charged to expense as incurred. Direct costs of constructing property and equipment are capitalized including interest costs related to construction.

Equipment held under capital leases is stated at the lower of the fair value of the asset or the net present value of the minimum lease payments at the inception of the lease. For equipment held under capital leases, depreciation is provided using the straight-line method over the shorter of the estimated useful lives of the leased assets or the related lease term.

The estimated useful lives of property and equipment are as follows:

Telecommunications networks and acquired bandwidth	3-20 years
Furniture, fixtures, equipment, and other	5-7 years
Leasehold improvements	the shorter of the estimated useful lives or the terms of the leases

These useful lives are determined based on historical usage with consideration given to technological changes and trends in the industry, which could impact the network architecture and asset utilization. Accordingly, in making this assessment, the Company considers its planned use of the assets, the views of experts within the Company and outside sources regarding the impact of technological advances and trends in the industry on the value and useful lives of its network assets. The Company periodically evaluates the estimated useful lives used to depreciate its assets. While the Company believes its estimate of useful lives are reasonable, significant differences in actual experience or significant changes in assumptions may affect future depreciation expenses.

(g) Broadband Wireless Licenses and Other Intangibles

Broadband wireless licenses are stated at their fair values at January 1, 2003. The Company is amortizing these licenses over the portion of the original license term remaining after the license is placed into service, or 10 years, whichever is shorter. Amortization commences when commercial service using broadband wireless technology is deployed in the license's geographic area.

Other intangible assets consist of customer relationships, internally developed technology and trade names. Customer relationships and internally developed technology are amortized using the straight-line method over the estimated useful lives of three years. The XO trade name was determined to have indefinite life and is not being amortized, but is reviewed at least annually for impairment in accordance with SFAS No. 142. Other trade names are amortized over their estimated useful lives of four years.

(h) Other Assets

Other assets consist primarily of a $25.0 million escrow as well as security deposits and pledged securities. The escrow and security deposits and pledged securities are stated at cost, and their fair value approximates their carrying value.

(i) Income Taxes

The Company accounts for income taxes in accordance with the provisions of SFAS No. 109, "Accounting for Income Taxes," ("SFAS No. 109") which requires that deferred income taxes are 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. Valuation allowances are used to reduce deferred tax assets to the amount considered likely to be realized.

(j) Class A Convertible Preferred Stock

The Company accretes changes in the redemption value of its Class A Convertible Preferred Stock as they occur and adjusts the carrying value of the security to equal the redemption value at the end of each reporting period. The accretion is included in net income (loss) applicable to common shares in the Company's consolidated statement of stockholders equity.

(k) Revenue Recognition

Revenues from telecommunications services are recognized when the services are performed, evidence of an arrangement exists, the fee is fixed and determinable and collectibility is probable. In circumstances when these criteria are not met, revenue recognition is deferred until resolution occurs.

Service discounts and incentives related to telecommunication services are recorded as a reduction of revenue when granted or ratably over a contract period. Fees billed in connection with service installations and other non-recurring charges are deferred and recognized ratably over the estimated customer life of three years.

The Company establishes allowances for collection of doubtful accounts and other sales credit adjustments. Allowances for sales credits are established through a charge to revenue, while allowances for doubtful accounts are established through a charge to selling, operating and general expense. The Company assesses the adequacy of these reserves monthly by considering general factors, such as the length of time individual receivables are past due, historical collection experience, the economic and competitive environment, and changes in the creditworthiness of its customers. The Company believes that the established valuation allowances are adequate. If circumstances relating to specific customers change or economic conditions worsen such that the Company's past collection experience and assessment of the economic environment are no longer relevant, XO's estimate of the recoverability of its trade receivables could be further reduced.

Revenue from the sale or lease of unlit network capacity is recognized upon consummation of the transaction and the acquirer's acceptance of the capacity in instances when the Company receives upfront cash payments and is contractually obligated to transfer title to the specified capacity at the end of the contract term. If the transaction does not meet these criteria, revenue is recognized ratably over the contract term. There were no sales of unlit capacity during the reported periods whereby revenue was recognized "up front" upon consummation of the transaction.

(l) Cost of Service

Cost of service includes expenses directly associated with providing telecommunications services to customers, including, among other items, the cost of connecting customers to the Company's networks via leased facilities, the costs of leasing components of our network facilities and costs paid to third party providers for interconnect access and transport services. All such costs are expensed as incurred. The Company accrues for the expected costs of services received from third party telecommunications providers during the period the services are rendered. Invoices received from the third party telecommunications providers are often disputed due to billing discrepancies.

The Company accrues for all disputed invoiced amounts as these amounts represent contingent liabilities that are considered probable and measurable and typically must pay the invoiced amounts even while they're being disputed. Disputes resolved in the Company's favor may reduce cost of service in the period the dispute is settled. Because the period of time required to resolve these types of disputes often lapses over several quarters, any benefits associated with the favorable resolution of such disputes normally are realized in periods subsequent to the accrual of the disputed invoice.

(m) Net Income (Loss) Per Share

Net income (loss) per common share, basic and diluted, is computed by dividing net income (loss) applicable to common shares by the weighted average number of common shares outstanding for the period. In periods of net loss, the assumed common share equivalents for options and warrants are anti-dilutive.

(n) Stock-Based Compensation

Effective January 1, 2003, the Company adopted the disclosure provisions of SFAS No. 148, "Accounting for Stock-Based Compensation-Transition and Disclosure," ("SFAS No. 148"). As allowed by SFAS No. 148, the Company has chosen to continue to account for compensation cost associated with its employee stock plan in accordance with the intrinsic value method prescribed by APB No. 25, "Accounting for Stock Issued to Employees," ("APB No. 25") adopting the disclosure-only provisions of SFAS No. 123. Under this method, no compensation expense is recorded if stock options are granted at an exercise price equal to or greater than the fair market value of the Company's stock on the grant date. If the Company had adopted the fair value method of accounting for its stock awards, stock-based compensation would have been determined based on the fair value for all stock awards at the grant date using a Black-Scholes pricing model and the following weighted average assumptions:

			Predecessor XO
	2004	2003	2002
Expected volatility	61.0%	75.0%	125.0%
Risk free interest rate	3.14%	2.6%	4.0%
Dividend yield	0.0%	0.0%	0.0%
Expected life (range in years)	4.0	4.0	4.0
Fair value per share at grant date	$ 2.19	$ 2.95	$0.11

The Company's pro forma net loss applicable to common shares, and pro forma net loss per common share, basic and diluted, if the Company had used the fair value method would have been as follows (dollars in thousands, except per share data):

			Predecessor XO
	December 31, 2004	December 31, 2003	December 31, 2002
Net loss applicable to common shares, as reported	$ (405,543)	$ (102,554)	$ (3,350,362)
Add: Stock-based employee compensation expense included in net loss applicable to common shares, as reported	406	708	28,928
Deduct: Total stock-based employee compensation expense determined under fair value based methods for all stock awards	(7,966)	(16,189)	(1,462)
Pro forma net loss	$ (413,103)	$ (118,035)	$ (3,322,896)
Net loss per common share, basic and diluted:			
Net loss per common share, basic and diluted — as reported	$ (2.57)	$ (1.07)	$ (7.58)
Net loss per common share, basic and diluted — pro forma	$ (2.58)	$ (1.23)	$ (7.52)

(o) Comprehensive Loss

Comprehensive loss includes the Company's net loss applicable to common shares, as well as net unrealized gains and losses on available-for-sale investments and, for any periods prior to the second quarter of 2002, foreign currency translation adjustments relating to the Company's European operations, which were disposed of in February 2002.

(p) Concentration of Credit Risk

Other financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of trade receivables. Although the Company's trade receivables are geographically dispersed and include customers in many different industries, a portion of the Company's revenue is generated from services provided to other telecommunications service providers. Several of these companies have filed for protection under Chapter 11 of the Bankruptcy Code while others have experienced business downturns. The Company believes that its established valuation and credit allowances are adequate to cover these risks.

(q) Fair Value of Financial Instruments

SFAS No. 107, "Disclosure about Fair Value of Financial Instruments" ("SFAS No. 107"), requires disclosure of fair value information about financial instruments, for which it is practicable to estimate the value. The carrying amounts for the majority of the Company's financial instruments classified as current assets and liabilities approximate their fair value due to their short maturities. Marketable securities are recorded at fair value. Amounts outstanding under long-term debt agreements approximate their estimated fair values as they accrue interest at rates that are variable every 3-6 months.

(r) Recent Accounting Pronouncements

Statement No. 123 (revised 2004), "Share-Based Payment" ("SFAS No. 123R"), was issued in December 2004. Once effective this statement will require entities to recognized compensation cost for all equity-classified awards granted, modified or settled after the effective date using the fair-value measurement method. In addition, public companies will recognize compensation expense for the unvested portion of awards outstanding as of the effective date based on their grant-date fair value as calculated under the original provisions of SFAS No. 123. The effective date for public entities is June 15, 2005. The amount of compensation expense that XO records after the adoption of SFAS No. 123R in 2005 and beyond, will depend on the amount, timing and pricing of stock option grants.

4. MARKETABLE SECURITIES AND OTHER INVESTMENTS

The amortized cost, gross unrealized gains and losses and fair value of the investment securities available-for-sale as of December 31, 2004 and 2003, are in the following table. Other investments consist of debt securities as of December 31, 2004 that mature in 2007 and 2008 (dollars in thousands):

	Fair Value	Cost Basis	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses
As of December 31, 2004				
Equity securities	$ 6,417	$ 1,705	$ 4,712	$ —
Debt securities	10,883	10,883	—	—
Total marketable securities	$ 17,300	$ 12,588	$ 4,712	$ —
As of December 31, 2003				
Equity securities	$ 30,041	$ 28,663	$ 3,001	$ (1,623)
Debt securities	12,011	12,011	—	—
Total marketable securities	$ 42,052	$ 40,674	$ 3,001	$ (1,623)

As part of the purchase effort with Allegiance, XO acquired $92.5 million in face value of unsecured Allegiance debt securities for $36.4 million. Consequently, XO is a claimant in Allegiance's bankruptcy. The ATLT will eventually settle all outstanding claims against the Allegiance estate with cash or the XO common stock that was distributed to it on the Closing Date. Based on our best estimate of XO's share of the net assets of the ATLT as disclosed in the latest report that the ATLT filed with the Bankruptcy Court, a $10.4 million impairment adjustment has been recorded as the decline in fair value was considered to be other than temporary. It is difficult to assess how much of the claim XO will recover, or when the recovery will be paid. This assessment could change based upon the total amount of claims the ATLT is directed to pay, the amount of administrative costs that it incurs and the value of its assets, including 45.4 million shares of XO's stock.

5. PROPERTY AND EQUIPMENT

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

	December 31, 2004	December 31, 2003
Telecommunications networks and acquired bandwidth	$ 675,844	$ 382,854
Furniture, fixtures, equipment, and other	236,788	77,783
	912,632	460,637
Less accumulated depreciation	208,032	79,501
	704,600	381,136
Construction-in-progress and inventory	115,936	104,848
	$ 820,536	$ 485,984

During 2004, 2003 and 2002, depreciation expense was $140.1 million, $83.1 million, and $598.5 million, respectively. During 2004, 2003 and 2002 the Company capitalized interest on construction costs of $4.0 million, $3.0 million, and $11.1 million, respectively. Assets classified as construction-in-progress and inventory are not being depreciated as they are not currently ready for their intended use and have not yet been placed into service.

6. BROADBAND WIRELESS LICENSES AND OTHER INTANGIBLES

Broadband wireless licenses and other intangible assets consisted of the following (dollars in thousands):

	December 31, 2004	December 31, 2003
Broadband wireless licenses	$ 59,508	$ 59,508
Customer relationships	112,366	49,987
Internally developed technology	9,521	9,521
Acquired tradenames	5,673	—
	187,068	119,016
Less accumulated amortization	(63,864)	(26,163)
	123,204	92,853
XO Trade name — indefinite life asset	16,662	16,662
	$ 139,866	$ 109,515

Amortization expense for the years ended December 31, 2004, 2003 and 2002 was $37.7 million, $26.2 million and $101.3 million, respectively. As of December 31, 2004, approximately $23.5 million of broadband wireless licenses are not being amortized as commercial services have not been deployed in the license's geographic area. Estimated amortization expense for the next five years is $48.4 million, $28.5 million, $17.7 million, $4.9 million and $0.1 million, respectively.

7. ACCRUED LIABILITIES

Accrued liabilities consisted of the following components (dollars in thousands):

	December 31, 2004	December 31, 2003
Accrued compensation	$ 54,405	$ 46,124
Deferred revenue	53,556	26,011
Accrued operating taxes	50,277	49,046
Accrued operating expenses	31,937	27,837
Accrued telecommunications costs	24,881	19,491
Accrued restructuring charges	13,776	20,046
Other accrued liabilities	12,700	19,798
	$ 241,532	$ 208,353

8. ACCOUNTING FOR ASSET RETIREMENT OBLIGATIONS

The Company has various agreements in which it leases conduit space and pole attachment rights from governmental entities, public utilities, and other telecommunications service providers for its fiber. Additionally, the Company has its telecommunications and data center equipment in various leased technical facilities. In many cases, the Company has contractual obligations to remove the assets associated with these lease agreements upon termination of the agreements. Accordingly, the Company has recorded a liability and asset for the present value of the estimated future capital expenditures associated with the related asset retirement obligations. The following table is a reconciliation of the beginning and ending asset retirement obligations (dollars in thousands):

Balance as of December 31, 2003	$ 12,855
Accretion	776
Revisions	(7,738)
Balance as of December 31, 2004	$ 5,893

The asset retirement obligations and associated asset are estimated based on several assumptions. If information becomes known that is different than the assumptions in use, revisions are made using the more precise information. If actual results differ from the assumptions used, the amount of the obligations will differ, perhaps significantly, from the amounts reflected in the accompanying consolidated financial statements.

9. LONG-TERM DEBT

The Company has a secured credit facility (the "Credit Facility") which matures on July 15, 2009. There are no additional borrowings available under the Credit Facility. At December 31, 2004, more than 90% of the underlying loans of the Credit Facility are held by an entity controlled by Mr. Carl C. Icahn, Chairman of the Company's Board of Directors ("Mr. Icahn"). At December 31, 2004, long-term debt consisted of $361.0 million in principal and $5.2 million of accrued interest that, if not paid, converts to principal. The Company paid down the Credit Facility by $197.6 million in January 2004. There are no current debt service requirements since cash interest payments as well as automatic and permanent quarterly reductions on the principal amount outstanding do not commence until 2009. However, in the event that consolidated excess cash flow (as defined in the Credit Facility) for any fiscal quarter during the term of the agreement is greater than $25.0 million, at the request of the lender, the Company will pay an amount equal to 50% of such excess cash flow greater than $25.0 million toward the reduction of outstanding indebtedness. In addition, if the ratio of XO's consolidated earnings before interest, taxes, depreciation and amortization ("EBITDA") to consolidated interest expense for four consecutive quarters exceeds 4:1, XO would be required to pay cash interest, unless waived by the lenders.

The security for the Credit Facility consists of all assets of XO including the stock of its direct and indirect subsidiaries, and substantially all the assets of those subsidiaries. The Credit Facility limits additional indebtedness, liens, dividend payments and certain investments and transactions, and contains certain covenants with respect to EBITDA requirements, as the term EBITDA is defined in the Credit Facility, and maximum capital expenditures. In addition, the Company was required to achieve a minimum consolidated EBITDA of not less than $62.0 million for the twelve-month period ended December 31, 2004, which requirement was not met by the Company. On August 3, 2004 the lender waived the applicability of the minimum EBITDA covenant for each quarter from March 31, 2004 through December 31, 2005. The Credit Facility has various contractual financial covenants, which XO did not meet in 2004 and for which XO has obtained waivers through December 31, 2005. If XO is not able to do any of the following by May 10, 2005 (i) amend the Credit Facility covenants, (ii) obtain an extension on the current waivers to at least March 31, 2006, or (iii) repay the Credit Facility with a new debt or equity offering, so that XO is in compliance, under the current accounting guidelines, XO will be required to reclassify the $366.2 million amount outstanding from long term to short term in its March 31, 2005 Form 10-Q. While the existing waivers prevent the lenders under the Credit Facility from demanding payment until March 31, 2006, this reclassification would cause a significant deterioration to XO's disclosed working capital and financial position. The Company is also required under the terms of the Credit Facility to maintain an unrestricted cash balance of $25.0 million at the end of each fiscal quarter.

The Company obtained on the Closing Date the waiver and consent of the lenders with respect to the following covenants contained in the Credit Facility and subject to XO providing updated collateral descriptions and legal opinions not later than November 22, 2004: (i) the $25.0 million limitation on the incurrence of permitted indebtedness, permitted equipment financings, acquired debt, and capital leases; (ii) the limitation on the incurrence of additional liens with respect to liens on the Allegiance assets that remained in place following the effective date of the Allegiance plan of reorganization; (iii) the restriction on making acquisitions in excess of $50.0 million; (iv) the requirement that accounts acquired as part of the Allegiance acquisition be subject to control agreements until November 22, 2004; and (v) any noncompliance arising from the entering into of an Operating Agreement with Allegiance.

As discussed above, the Company is not required to pay cash interest accrued on the principal amount under the Credit Facility until it meets certain financial ratios; however, the Company can elect to begin paying interest in cash prior to the required date. Loans under the Credit Facility bear interest, at the Company's option, at an alternate base rate, as defined, or a Eurodollar rate plus, in each case, applicable margins. Once the Company begins to pay accrued interest in cash, the applicable margins are reduced. At December 31, 2004, the annualized weighted average interest rate applicable to outstanding borrowings under the Credit Facility was 7.77%.

10. CONVERTIBLE PREFERRED STOCK

On August 6, 2004, XO completed a private placement of 4.0 million shares of its 6% Class A Convertible Preferred Stock (the "Preferred Stock Offering") for net proceeds of $199.4 million. Affiliates of Mr. Icahn purchased 95% of the preferred shares sold in the Preferred Stock Offering, and an affiliate of Amalgamated Gadget, L.P., holder of approximately 8% of XO's outstanding common stock, purchased the remaining five percent. As of December 31, 2004, the liquidation and redemption value of the 6% Class A Convertible Preferred Stock was $204.4 million.

The Preferred Stock Offering was reviewed and approved by a special committee of XO's Board of Directors consisting of XO's three independent directors, Messrs. Dell, Gradin and Knauss. The special committee selected its own counsel and financial advisor. The financial advisor advised the special committee that, subject to specified qualifications, assumptions and limitations, the material terms of the 6% Class A Convertible Preferred Stock were fair to XO, from a financial point of view, at the time of issuance. Proceeds of the Preferred Stock Offering will be used for general working capital purposes and to fund possible future acquisitions that would add additional scale and synergies to XO's business.

The Class A Preferred Stock ranks senior to the Company's common stock. Holders of the Class A Preferred Stock are not entitled to receive annual dividends, however, the liquidation preference of the Class A Preferred Stock automatically increases at a rate of 1.5% each quarter through the maturity date, January 15, 2010. The Company is required to redeem the then-outstanding shares of Class A Preferred Stock on the maturity date at 100% of their aggregate liquidation preference, including compounded accretion through that date, unless earlier redeemed or converted into common stock. If all of the shares of Class A Preferred Stock were to remain outstanding on the maturity date, and assuming the accretion of all the required increases to the liquidation preference thereof, holders of the Class A Preferred Stock would be entitled to 59,868,561 shares of common stock and would have an aggregate liquidation preference of approximately $276.6 million. The shares of Class A Preferred Stock are convertible into common stock based on a share price of $4.62, a premium of approximately 20% above the trading price of the common stock on the closing date of the Preferred Stock Offering. The Company may also, at its sole option, redeem the Class A Preferred Stock at any time after the third anniversary of the issue date of such shares if the average market price of the Company's common stock for the 20 days prior to such redemption is equal to or greater than 250% of the conversion price of the Class A Preferred Stock. Each holder of the Class A Preferred Stock is entitled to one vote for each share of common stock issuable upon the conversion of the shares of Class A Preferred Stock as of the record date for such stockholders vote. Both the conversion ratio and the voting power of each share of Class A Preferred Stock will be automatically increased each quarter as the liquidation preference increases at the rate of 1.5% each quarter. The holders of Class A Preferred Stock also have anti-dilution protection in the event that the Company issues shares of common stock at a price below the then-prevailing market price of the Company's common stock.

11. STOCKHOLDERS' EQUITY

The Company initiated a rights offering (the "Rights Offering") during the fourth quarter of 2003 offering 40.0 million shares of its common stock at a price of $5.00 per share. The Rights Offering closed on January 5, 2004. An aggregate of 39.7 million shares were issued, yielding net proceeds of $197.6 million.

XO has warrants outstanding to purchase up to an additional 23.75 million shares of its common stock. The warrants consist of:

- Series A Warrants to purchase 9.5 million shares of XO common stock at an exercise price of $6.25 per share;
- Series B Warrants to purchase approximately 7.1 million shares of XO common stock at an exercise price of $7.50 per share; and
- Series C Warrants to purchase approximately 7.1 million shares of XO common stock at an exercise price of $10.00 per share.

The warrants were valued at issuance at approximately $44.9 million using a Black Scholes model and are included in XO's common stock in the accompanying consolidated balance sheet. The warrants will expire 7 years after the date of issuance or in 2010. The exercise price applicable to each respective series of warrants is subject to adjustment in certain events.

In addition to the outstanding warrants discussed above, the Company has a stock option plan that can further dilute investors if exercised. This stock option plan is discussed further in note 13. See note 17 for related party disclosure on XO's stockholder's equity.

12. INCOME TAXES

As of December 31, 2004, XO had net operating loss carryforwards of approximately $2.50 billion, of which $1.08 billion related to the acquisition of the Acquired Businesses. The acquired net operating loss carryforwards expire between 2011 and 2023. The remainder of XO's net operating loss carryforwards expire between 2023 and 2024. Use of the Acquired Businesses net operating loss carryforward is significantly limited due to the limitations imposed under the ownership change rules in the U.S. Internal

Revenue Code. XO's use of the surviving capital loss carryforward of $0.2 billion, which expires in 2005, is also subject to limitations imposed under the ownership change rules in the U.S. Internal Revenue Code. The utilization of the expected tax benefit from property and equipment depreciation could also be impacted by the ownership change rules of the U.S. Internal Revenue Code.

XO was a member of the affiliated group of corporations controlled by Mr. Icahn in filing a consolidated federal income tax return from January 2003 through January 2004, when Mr. Icahn's ownership percentage fell below the amount required by the Internal Revenue Code for the filing of consolidated returns. As such, in January 2004, XO deconsolidated with Starfire Holding Corporation ("Starfire"), the Parent entity of the affiliated group of corporations controlled by Mr. Icahn. XO had entered into a Tax Allocation Agreement with Starfire in January 2003 which provides that while XO files on a consolidated basis with Starfire, Starfire will pay all consolidated federal income taxes on behalf of the consolidated group that includes XO, and XO will make payments to Starfire in an amount equal to the tax liability, if any, that it would have had if it were to file as a group separate and apart from Starfire. Upon deconsolidation, the Tax Allocation Agreement generally provides that Starfire will reimburse XO each year going forward for the excess of XO's actual income tax expense over the income tax that XO would have owed if net operating losses or other tax attributes used in prior periods by the Starfire consolidated group were still available to XO. XO's net operating loss carryforward has been reduced by the amount used by Starfire in 2003. No amount has been recorded for the potential reimbursements from Starfire under the Tax Allocation Agreement.

The provisions of SFAS No. 109 have been applied as if the Company were a separate taxpayer. As reflected in the following table, XO established a valuation allowance against the deferred tax assets of $2,021 million and $1,541 million as of December 31, 2004 and 2003, respectively. A majority of the $480 million valuation increase from 2003 to 2004 relates to the acquisition of net operating losses from the Acquired Businesses. Valuation allowances are used to reduce deferred tax assets to the amounts considered likely to be realized. Components of deferred tax assets and liabilities were as follows (dollars in thousands):

	December 31, 2004	December 31, 2003
Deferred tax assets:		
Provisions not currently deductible	$ 108,959	$ 172,368
Property, equipment and other long-term assets (net)	820,885	893,957
Net operating loss and capital loss carryforwards	1,109,575	483,453
Total deferred tax assets	2,039,419	1,549,778
Valuation allowance	(2,021,103)	(1,540,612)
Net deferred tax assets	18,316	9,166
Deferred tax liabilities:		
Other identifiable intangibles	(25,147)	(15,997)
Total deferred tax liabilities	(25,147)	(15,997)
Net deferred tax liability	$ (6,831)	$ (6,831)

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

	XO 2004	XO 2003	Predecessor XO 2002
Statutory U.S. federal rate	35.0%	35.0%	35.0%
State income taxes, net of federal benefit	6.0%	6.0%	6.0%
Valuation allowance for deferred tax assets	(22.6%)	(41.0%)	(18.3%)
Impairment	(18.4%)	—%	(22.7%)
Effective income tax rate	—%	—%	—%

13. STOCK COMPENSATION ARRANGEMENTS

The XO Communications, Inc. 2002 Stock Incentive Plan ("the 2002 Stock Incentive Plan") was adopted in January 2003. Under the 2002 Stock Incentive Plan, the Company is authorized to issue awards for up to 17.6 million shares of its common stock in the form of restricted stock or options to purchase stock. The 2002 Stock Incentive Plan is administered by the Compensation Committee of the Company's Board of Directors, which has the discretionary authority to determine all matters relating to awards of stock options and restricted stock, including the selection of eligible participants, the number of shares of common stock to be subject to each option or restricted stock award, the exercise price of each option, vesting, and all other terms and conditions of awards. Unless the Compensation Committee designates otherwise, all options expire on the earlier of (i) ten years after the date of grant, (ii) twelve months after termination of employment with XO due to death or complete and permanent disability, (iii) immediately upon termination of employment by XO for cause, or (iv) three months after termination of employment by the employee or by XO for other than cause.

In June 2003, XO filed a registration statement covering the offer and sale of stock options and stock appreciation rights ("SARs") to be granted in conjunction with the 2003 Employee Retention and Incentive Plan (the "Retention Plan") for an aggregate award of 1.9 million shares of its common stock (the "Retention Plan Awards"). The financial goals and the terms of the Retention Plan were established by the Company's Board of Directors. The per share exercise price for the Retention Plan Awards was set at $5.84. Any compensation was recorded as deferred compensation and amortized to on a straight line basis expense based on the associated vesting period.

The following two tables summarize information regarding option activity under the 2002 Stock Option Plan for the years ended December 31, 2003 and 2004:

	Number of Shares	Weighted Average Exercise Price
Outstanding at January 1, 2003.	—	$ —
Granted	15,394,162	$ 5.09
Canceled	(3,697,068)	$ 5.02
Exercised	(1,274,139)	$ 5.01
Outstanding at December 31, 2003.	10,422,955	$ 5.12
Exercisable, at December 31, 2003.	2,424,903	$ 5.10
Outstanding at December 31, 2003.	10,422,955	$ 5.12
Granted	3,577,382	$ 5.26
Canceled	(2,184,093)	$ 5.55
Exercised	(556,429)	$ 5.01
Outstanding at December 31, 2004.	11,259,815	$ 5.09
Exercisable, at December 31, 2004.	3,726,298	$ 5.02

		Options Outstanding			Options Exercisable	
	Range of Exercise Prices	Options Outstanding at December 31,	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Options Exercisable at December 31,	Weighted Average Exercise Price
2003	$ 4.80 – $7.05	10,422,955	9.1	$ 5.12	2,424,903	$ 5.10
2004	$ 4.80 – $7.05	11,259,815	8.6	$ 5.09	3,726,298	$ 5.02

14. SUPPLEMENTAL DISCLOSURE

Cash flows

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

	Year Ended December 31, 2004	Year Ended December 31, 2003	Predecessor XO Year Ended December 31, 2002
Non-cash financing and investing activities were as follows:			
Stock issued for acquired businesses	$ 311,306	$ —	$ —
Assets and obligations acquired through capital leases	3,932	—	—
Conversion of accrued interest to long-term debt	28,746	29,901	—
Cash paid for interest	$ 2,481	$ 2,315	$ 11,681

Employee Savings and Retirement Plan

At December 31, 2004, the Company had a defined contribution plan, generally covering all full time employees in the United States. The Company provides a match to all eligible employees based on certain plan provisions and the discretion of the Board of Directors. The Company makes a 50% matching contribution up to 5% of the participant's compensation. Company contributions net of forfeitures were $2.3 million, $4.8 million and $7.0 million during 2004, 2003 and 2002, respectively.

15. OPERATING SEGMENTS

Reportable Segments

The Company operates its business as one telecommunications segment. The Company's communications segment includes all of its services including voice services, data services and integrated voice and data services. These services have similar network assets, operations, and technology requirements and are sold through similar sales channels to a similar targeted customer base. Therefore, the Company manages these services as a single segment that are sold in geographic areas, or markets, within the United States.

Products and Services

The Company classifies its services revenues offered by its telecommunications segment into voice services, data services and integrated voice and data services (dollars in thousands):

	Year Ended December 31, 2004	Year Ended December 31, 2003	Predecessor XO Year Ended December 31, 2002
Voice services	$ 673,318	$ 572,774	$ 659,558
Data services	414,782	392,742	472,247
Integrated voice and data services	212,320	144,967	128,048
Total revenue	$ 1,300,420	$ 1,110,483	$ 1,259,853

16. SELECTED QUARTERLY DATA (Unaudited)

Quarterly financial information is summarized in the table below (dollars in thousands, except per share data):

	Quarter ended 2004 (a)			
	March 31,	June 30,	September 30,	December 31,
Revenue	$ 260,945	$ 278,183	$ 391,885	$ 369,407
Cost of service	109,961	118,822	161,946	162,006
Loss from operations(c)	(43,266)	(34,853)	(36,227)	(255,946)
Net loss	(48,494)	(43,820)	(41,779)	(271,450)
Net loss applicable to common shares	(48,494)	(43,820)	(43,619)	(274,520)
Net loss per common share (basic and diluted)	(0.37)	(0.31)	(0.24)	(1.51)

	Quarter ended 2003			
	March 31,	June 30,	September 30,	December 31,
Revenue	$ 286,093	$ 283,918	$ 279,433	$ 261,039
Cost of service	107,506	104,898	106,935	102,790
Loss from operations	(14,015)	(13,260)	(35,878)	(48,705)
Net loss(b)	(20,488)	(19,836)	(40,787)	(21,443)
Net loss applicable to common shares	(20,488)	(19,836)	(40,787)	(21,443)
Net loss per common share (basic and diluted)(b)	(0.22)	(0.21)	(0.42)	(0.22)

(a) The 2004 results include the results of the Acquired Businesses from June 23, 2004 through December 31, 2004.

(b) Fourth quarter of 2003 includes a $33.5 million realized investment gain.

(c) Fourth quarter of 2004 includes a $212.5 million non-cash goodwill impairment charge.

17. RELATED PARTY TRANSACTIONS

Various entities controlled by Mr. Icahn hold the following interests in XO:

	Outstanding Common Stock	Series A, B and C Warrants	Credit Facility	Preferred Stock
At December 31, 2004	Greater than 50%	Greater than 40%	Greater than 90%	95%

In August 2004, after the closing of the Preferred Stock Offering, Mr. Icahn filed a schedule 13D amendment with the Securities and Exchange Commission disclosing that his beneficial ownership, as defined therein, was 60.7% of XO. As a result of his majority ownership, Mr. Icahn can elect all of XO's directors, who in turn appoint the members of the committees of XO's Board of Directors, appoint key members of XO's executive management team, and appoint XO's auditors. Currently, Mr. Icahn is Chairman of the Board of Directors and three employees of Icahn Associates also sit on the Board of Directors and various Committees of the Board of Directors. Under applicable law and XO's Certificate of Incorporation and by-laws, certain action cannot be taken without the approval of holders of a majority of XO's voting stock, including, without limitation, mergers, acquisitions, the sale of substantially all XO's assets, and amendments to XO's Certificate of Incorporation and by-laws.

Mr. Icahn, through various entities that he controls, has the right to require XO to register, under the Securities Act of 1933, shares of XO's common stock held by such entities and to include shares of XO's common stock held by them in certain registration statements filed by XO.

Dixon Properties, LLC ("Dixon"), which is controlled by Mr. Icahn, owns the building in which XO's headquarters is located. XO currently leases approximately 170,000 square feet of space in that building. Pursuant to the lease agreement, XO has paid $3.5 million in lease rent to Dixon for the year ended December 31, 2004 and XO is obligated to pay approximately $12.1 million to Dixon through the expiration of the initial term of the lease, which is November 30, 2007.

XO has entered into a Tax Allocation Agreement with an Icahn affiliate, that is more fully discussed in note 12.

The Company provides certain telecommunications services to companies affiliated with Mr. Icahn. For the year ended December 31, 2004, the total revenue recognized on such services affiliated with Mr. Icahn was approximately $2.0 million. The Company has purchased approximately $0.6 million in services from Icahn affiliates during 2004. During 2004, XO purchased approximately $1.0 million in hardware and services from Dell Computers, Inc. Mr. Adam Dell, an XO director, is the brother of Mr. Michael Dell, the Chairman of Dell, Inc.

XO provided telecommunications services to Allegiance from February 18, 2004 through the Closing Date. Total revenue recognized for those services was approximately $1.7 million. In addition, XO provided Allegiance management services under an Operating Agreement between April 13, 2004 and the Closing Date. XO believes it is owed monies under the terms of the Operating Agreement and this is part of the total claim that is discussed in note 2. Based on the contingent nature of this claim, it is not recorded in the accompanying consolidated financial statements.

On June 8, 2004 XO entered into a Registration Rights Agreement with the ATLT, holder of approximately 24.9% of XO's outstanding common stock, pursuant to which XO agreed to utilize its best efforts to register for public resale, the 45,380,000 shares of XO common stock issued as part of the acquisition of the Acquired Businesses. XO has not filed such registration statement.

On November 2, 2004, XO entered into an Indemnification Agreement with each of Mr. Dell, Robert L. Knauss and Fredrik Gradin, each of whom is an independent member of XO's Board of Directors, pursuant to which XO has agreed to indemnify each of such directors for any personal liability and costs that he may incur in connection with the performance of services as a director of XO, and advance to each such director any expenses that he may incur in connection with any litigation or actions related to such services.

18. COMMITMENTS AND CONTINGENCIES

Operating Commitments

The Company is leasing premises under various noncancelable operating leases for administrative space, building access, and other 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 2029. The Company also has various noncancelable long-term contractual obligations associated with maintenance and service agreements.

Future minimum lease commitments required under noncancelable operating leases and contractual obligations are as follows (dollars in thousands):

Year Ending December 31,	Operating lease obligations	Other long-term contractual obligations
2005	$ 70,822	$ 61,273
2006	66,657	52,521
2007	61,527	48,806
2008	51,394	47,524
2009	43,257	33,679
Thereafter	168,235	95,787
Total minimum commitments	$ 461,892	$ 339,590

Rent expense for cancelable and noncancelable leases totaled approximately $57.4 million, $53.7 million, and $76.4 million for the years ended December 31, 2004, 2003, and 2002, respectively. The minimum lease payments noted above have not been reduced for sublease income totaling approximately $0.7 million for the year ended December 31, 2004.

Capital Leases

Network assets under capital leases totaled approximately $9.3 million and $1.4 million as of December 31, 2004 and 2003, respectively, and are included in telecommunications networks in property and equipment. Depreciation on leased assets of $0.4 million for each of the years ended December 31, 2004 and 2003 is included in depreciation expense. Future minimum lease payments under capital lease obligations as of December 31, 2004 are as follows (dollars in thousands):

Year Ending December 31,	
2005	$ 4,789
2006	4,537
2007	3,854
2008	2,398
2009	1,770
Thereafter	13,681
Total minimum capital lease payments	31,029
Less: imputed interest	(10,814)
Less: current portion of capital lease obligations	(2,820)
Long-term portion of capital lease obligation	$ 17,395

The Company provides intercity transport primarily through five year leases of wavelength capacity that were paid for at the beginning of the term. The first of these leases expires in 2006. At that time, XO will either renew these leases or light its intercity fiber network, either of which will be a substantial capital commitment.

Legal Proceedings

In addition to the litigation disclosed in note 2, XO is involved in lawsuits, claims, investigations and proceedings consisting of commercial, regulatory, securities, tort, and employment matters, which arise in the ordinary course of business. In addition, disputes with respect to general unsecured claims and one administrative expense claim in the amount of approximately $2.1 million, remain pending from the Company's Chapter 11 proceedings. In accordance with SFAS No. 5, "Accounting for Contingencies," XO makes a provision for a liability when it is both probable that a liability has been incurred and the amount of the loss can be reasonably estimated. XO believes it has adequate provisions for any such matters. XO reviews these provisions at least quarterly and adjusts these provisions to reflect the impacts of negotiations, settlements, rulings, advice of legal counsel, and other information and events pertaining to a particular case. Litigation is inherently unpredictable. However, XO believes that it has valid defenses with respect to legal matters pending against it. Nevertheless, it is possible that cash flows or results of operations could be materially affected in any particular period by the unfavorable resolution of one or more of these contingencies.

19. RESTRUCTURING CHARGES AND ASSET WRITE-DOWNS

During 2003, the Company recorded restructuring charges from the reduction of its work force and estimated losses associated with restructured leases. A restructuring charge was recorded during the first half of 2002 when the Company implemented a plan to restructure certain of its business operations. The restructuring plan included divesting its European operations and reducing the Company's discretionary spending, capital expenditures and workforce.

As of December 31, 2004, the remaining restructuring accrual was $43.7 million, which relates primarily to payments due to landlords on exited leased facilities. The restructuring accrual has decreased from $60.0 million as of December 31, 2003, mainly due to $13.3 million in payments associated with exited leased facilities.

20. REORGANIZATION

On January 16, 2003 (the "Effective Date"), XO's holding company ("XO Parent") consummated its Plan of Reorganization and emerged from its Chapter 11 reorganization proceedings with a significantly restructured balance sheet. The consummation of the Plan of Reorganization resulted in the following changes in XO Parent's capital structure:

- The conversion of $1.0 billion of loans under its pre-petition secured credit facility into $500.0 million of outstanding principal amount under an amended and restated credit agreement;
- The extinguishment of all amounts due under its pre-petition unsecured senior and subordinated notes and certain general unsecured obligations;
- The cancellation of all outstanding shares and interests in its pre-petition preferred stock and pre-petition common stock; and
- The issuance of approximately 95.0 million shares of common stock of the reorganized Company and warrants to purchase up to an additional 23.75 million shares of the common stock of the reorganized Company.

The Company adopted the fresh start accounting provisions ("fresh start") of SOP 90-7 "Financial Reporting by Entities in Reorganization under the Bankruptcy Code", ("SOP 90-7") during the first quarter of 2003. Due to the immateriality of the results of operations for the period between January 1, 2003 and the Effective Date, the Company accounted for the consummation of the Plan of Reorganization as if it had occurred on January 1, 2003 and implemented fresh start reporting as of that date. Fresh start requires that the Company adjust the historical cost of its assets and liabilities to their fair value. The fair value of the reorganized Company of approximately $1.3 billion was determined based on the negotiated sum of the reorganized Company's liabilities and equity that were issued and outstanding after final negotiations and Bankruptcy Court approval. These included $500.0 million of debt outstanding under the Credit Facility, $475.0 million of XO's common stock, and $373.1 million of other liabilities that were not eliminated or discharged under the Plan of Reorganization.

Fresh start requires that the reorganization value be allocated to the entity's net assets in conformity with procedures specified by SFAS No. 141. The Company engaged an independent appraiser to assist in the allocation of the reorganization value to the reorganized Company's assets and liabilities by determining the fair market value of its property and equipment, intangible assets and certain obligations related to its facility leases. A reconciliation of the adjustments recorded in connection with effecting the Plan of Reorganization and adopting fresh start accounting is presented below (dollars in thousands):

	Predecessor XO December 31, 2002	Reorganization	Fresh Start Adjustments(d)	Reorganized XO January 1, 2003
ASSETS				
Current assets:				
Cash and cash equivalents	$ 314,038	$ —	$ —	$ 314,038
Marketable securities	246,945	—	—	246,945
Accounts receivable, net	116,541	—	—	116,541
Other current assets	83,480	—	(48,288)	35,192
Total current assets	761,004	—	(48,288)	712,716
Property and equipment, net	2,780,589	—	(2,304,001)	476,588
Broadband wireless licenses and other intangibles, net	984,614	—	(848,936)	135,678
Other assets, net	59,289	—	(36,181)	23,108
Total assets	$ 4,585,496	$ —	$ (3,237,406)	$ 1,348,090
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY				
Current liabilities:				
Accounts payable	$ 63,729	$ —	$ 3,539	$ 67,268
Accrued liabilities	266,102	—	(30,910)	235,192
Current liabilities subject to compromise	5,497,207	(5,466,667)(a)	(30,540)	—
Total current liabilities	5,827,038	(5,466,667)	(57,911)	302,460
Long-term debt	—	500,000(b)	—	500,000
Other long-term liabilities	75,242	—	(4,612)	70,630
Long-term liabilities subject to compromise	7,182	—	(7,182)	—
Total liabilities	5,909,462	(4,966,667)	(69,705)	873,090
Predecessor XO redeemable preferred stock — subject to compromise	1,708,316	(1,708,316)(a)	—	—
Stockholders' (deficit) equity:				
Predecessor XO common stock	4,628,139	—	(4,628,139)	—
Reorganized XO common stock and warrants	—	475,000(c)	—	475,000
Deferred compensation	(8,500)	—	8,500	—
Accumulated other comprehensive income	2,512	—	(2,512)	—
Accumulated deficit	(7,654,433)	6,199,983(e)	1,454,450	—
Total stockholders' (deficit) equity	(3,032,282)	6,674,983	(3,167,701)(e)	475,000
Total liabilities and stockholders' (deficit) equity	$ 4,585,496	$ —	$ (3,237,406)	$ 1,348,090

(a) To record the discharge of pre-petition indebtedness, including a $1.0 billion credit facility, $4.2 billion of senior and convertible subordinated notes, $245.2 million of accrued interest, and the elimination of $1.7 billion of pre-petition redeemable preferred stock and $50.6 million of accrued dividends, all in accordance with the Plan of Reorganization.

(b) To record the outstanding principal under the Credit Agreement, in accordance with the Plan of Reorganization.

(c) To record the issuance of 95.0 million shares of New Common Stock and warrants in accordance with the Plan of Reorganization. Participation in the Rights Offering was recorded in the first quarter of 2004.

(d) To adjust the carrying value of assets, liabilities and stockholders' equity to fair value, in accordance with fresh start.

(e) Net reorganization gain on January 1, 2003 consisted of the following (dollars in thousands):

Net gain resulting from reorganization of debt, preferred stock and equity	$ 6,199,983
Net loss resulting from fresh start fair value adjustments to assets and liabilities	(3,167,701)
Total reorganization gain, net	$ 3,032,282

21. SUBSEQUENT EVENTS (Unaudited)

On March 16, 2005, McLeodUSA Inc, ("McLeod") announced that it is looking into financial restructuring options due to its on-going cash requirements. XO currently holds McLeod debt securities that are included in marketable securities and other investments. It is too early to conclude what type of restructuring option McLeod will choose, or if any will be approved by their creditors and how that would impact our investment. Based on this announcement, there is a risk that the carrying value of $10.8 million will be impaired, and require adjustment in 2005.

XO Communications, Inc.

Schedule II — Consolidated Valuation and Qualifying Accounts
For The Years Ended December 31, 2004, 2003 and 2002

(dollars in thousands)	Beginning Balance	Reorganization Adjustments	Additions/ Reductions charged to expense	Reductions	Ending Balance
Allowance for doubtful accounts					
2002	$ 32,492	$ —	$ 53,631	$ (49,093)	$ 37,030
2003	$ 37,030	$ —	$ 29,998	$ (34,042)	$ 32,986
2004	$ 32,986	$ —	$ 34,898	$ (28,903)	$ 38,981
Restructuring accrual					
2002 (a)	$ 125,773	—	$ 480,168	$ (526,951)	$ 78,990
2003 (b)	$ 38,725	$ 26,809	$ 11,618	$ (17,176)	$ 59,976
2004	$ 59,976	$ —	$ (2,971)	$ (13,349)	$ 43,656

(a) Only $49.7 million of the reduction in 2002 restructuring accrual was for cash payments. The balance was associated with the non-cash asset write down resulting from an agreement with Level 3 to amend various agreements relating to XO's Level 3 intercity fiber network facilities.

(b) The beginning balance was adjusted to its fair value when we implemented fresh start.

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Exhibit 10.4

REGISTRATION RIGHTS AGREEMENT

REGISTRATION RIGHTS AGREEMENT, dated as of June 23, 2004, between Allegiance Telecom, Inc., ("Allegiance"), Allegiance Telecom Company Worldwide ("Allegiance Worldwide"), Allegiance Telecom Liquidating Trust (the "Trust", and together with Allegiance and Allegiance Worldwide, the "Allegiance Parties") and XO Communications, Inc., a Delaware corporation (the "Company").

RECITALS

WHEREAS, the Trust will acquire shares of Common Stock, par value $.01 per share, of the Company (the "Common Stock") to be issued pursuant to that certain Asset Purchase Agreement (the "Purchase Agreement"), dated as of February 18, 2004, between the Company and Allegiance as debtor-in-possession and Allegiance Worldwide as debtor-in-possession;

WHEREAS, pursuant to their Joint Plan of Reorganization of, confirmed by order of the Bankruptcy Court for the Southern District of New York on June 23, 2004, Allegiance and Allegiance Worldwide will transfer the Common Stock to the Trust established thereunder to hold, sell or distribute to their pre-petition creditors in accordance with its terms; and

WHEREAS, the Company has agreed, pursuant to the Stipulation and Order, entered on June 23, 2004, to grant the Trust registration rights upon the
terms and subject to the conditions hereinafter set forth; and

NOW, THEREFORE, in consideration of the foregoing premises and for other good and valuable consideration, the parties hereby agree as follows:

SECTION 1. DEFINITIONS. As used in this Agreement, the following terms have the respective meanings set forth below:

COMMISSION: shall mean the Securities and Exchange Commission or any other federal agency at the time administering the Securities Act;

EXCHANGE ACT: shall mean the Securities Exchange Act of 1934, as amended;

MARKET STAND-OFF PERIOD: has the meaning defined in Section 5(a).

PERSON: shall mean an individual, partnership,joint-stock company, corporation, trust or unincorporated organization, and a government or agency or political subdivision thereof;

REGISTER, REGISTERED and REGISTRATION: shall be deemed to refer to registration effected by preparing and filing a registration statement in compliance with the Securities Act (and any post-effective amendments filed or required to be filed) and the declaration or ordering of effectiveness of such registration statement;

<u>Exhibit D</u>

Press Release

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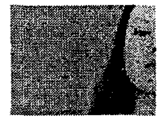

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November 04, 2005

Company Will Focus Business on Delivering Fixed Broadband Wireless Services to Businesses and Service Providers

National Wireline Telecommunications Business Will Continue as a Private Company Wholly-Owned by Affiliates of Carl Icahn

RESTON, VA - XO Communications, Inc. (OTCBB: XOCM.OB) today announced an agreement that will create a leading provider of fixed broadband wireless services to businesses and service providers. In order to create and finance the fixed wireless business, XO will sell its national wireline telecommunications business for $700 million in cash. Following the sale, the Company will retain its fixed broadband wireless spectrum assets and be uniquely positioned to be a leading provider of fixed broadband wireless services nationally as one of the largest holders of fixed wireless licenses in the 28 GHz-31 GHz spectrum range covering more than 70 U.S. major metropolitan markets.

"The action we take today will create a pure-play fixed broadband wireless provider that combines significant resources with in-depth industry expertise to meet the growing demand for high-bandwidth broadband wireless services," said XO CEO Carl Grivner. "The market opportunity to provide these services has emerged, and our new focus on fixed wireless communications will enable us to offer robust fixed wireless solutions to businesses, mobile phone companies, and wireline telecommunications companies."

The proceeds from the sale of the wireline business will be used to repay XO's outstanding long-term debt, to offer to redeem, at the closing of the sale, XO's outstanding preferred stock and to fund growth and development of the wireless business. Once the sale is completed, the wireless business will be debt-free and is currently expected to have in excess of $300 million in cash to fund its operations and for other corporate purposes. The Company's wireless services have already been made available to businesses and wireless service providers in select markets and, using its cash position and new strong balance sheet, the Company plans to launch its services on a wider basis in the near future. The transaction is anticipated to close in late 2005 or early 2006.

The agreement is the culmination of an extensive process established by the Company over a period of several months during which multiple bids for the wireline business of the Company were evaluated by a Special Committee of the Company's Board of Directors. The winning bidder was Elk Associates LLC, an entity owned by XO's controlling stockholder, Carl Icahn, which has executed a definitive agreement to purchase the wireline business. However, as provided in the definitive agreement, the Company and the Special Committee remain open to consideration of superior proposals from third parties in certain events, subject to paying Elk Associates a break-up fee of 1% of the consideration payable in the transaction in the event that the Company receives and determines to accept a superior proposal.

The Special Committee overseeing this process consists solely of non-management directors who are not affiliated with Mr. Icahn. The Special Committee led the negotiation of the terms of the agreement with Elk Associates LLC on behalf of the Company and, after receiving the opinion of the Company's financial advisor, Jefferies & Co., Inc., to the effect that the consideration to be received by the Company in the transaction is fair to the Company from a financial point of view, approved the agreement and recommended its approval by the Board of Directors of the Company. Completion of the transaction will be subject to a number of conditions, including shareholder approval. The description of the agreement contained herein is qualified in its entirety by reference to such agreement, which will be publicly filed as required under applicable securities laws.

The "XO Communications" brand name will be transferred to the private company and thereby will remain with the national wireline telecommunications business. XO anticipates operating its fixed wireless business under a new name.

It is anticipated that the wireless and wireline companies will enter into commercial agreements to sell each other's products and services at competitive rates in order to take advantage of market opportunities.

About XO Communications
XO Communications is a leading provider of national and local telecommunications services to businesses, large enterprises and telecommunications companies. XO offers a complete portfolio of services, including local and long distance voice, dedicated Internet access, private networking, data transport, and Web hosting services as well as bundled voice and Internet solutions. XO provides these services over an advanced, national facilities-based IP network and serves more than 70 metropolitan markets across the United States. For more information, visit www.xo.com.

FOR MORE INFORMATION CONTACT:

CHAD COUSER / XO COMMUNICATIONS
703-547-2746
CHAD.COUSER@XO.COM

FORWARD LOOKING STATEMENT NOTE
THE STATEMENTS CONTAINED IN THIS RELEASE THAT ARE NOT HISTORICAL FACTS ARE "FORWARD-LOOKING STATEMENTS" (AS SUCH TERM IS DEFINED IN THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995) THAT INVOLVE RISKS AND UNCERTAINTIES. THESE STATEMENTS INCLUDE THOSE DESCRIBING XO'S EXPECTED FUTURE BUSINESS AND NETWORK OPERATIONS AND RESULTS OF OPERATIONS, XO'S ABILITY TO SERVICE THE GROWING DEMAND FOR HIGH-BANDWIDTH BROADBAND WIRELESS SERVICES, XO'S ABILITY TO INCREASE SALES ONCE IT BEGINS

OPERATING UNDER A NEW NAME, AND XO'S ABILITY TO CONTINUE TO IMPLEMENT EFFECTIVE COST CONTAINMENT MEASURES. MANAGEMENT CAUTIONS THE READER THAT THESE FORWARD-LOOKING STATEMENTS ARE ONLY PREDICTIONS AND ARE SUBJECT TO RISKS AND UNCERTAINTIES AND ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THOSE INDICATED IN THE FORWARD-LOOKING STATEMENTS AS A RESULT OF A NUMBER OF FACTORS. THESE FACTORS INCLUDE, BUT ARE NOT LIMITED TO, THOSE RISKS AND UNCERTAINTIES DESCRIBED FROM TIME TO TIME IN THE REPORTS FILED BY XO COMMUNICATIONS, INC. WITH THE SECURITIES AND EXCHANGE COMMISSION, INCLUDING ITS ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2004 AND ITS QUARTERLY REPORTS ON FORM 10-Q.

Tariffs | P

<u>Exhibit E</u>

Proposed Price List

TITLE PAGE

LOCAL EXCHANGE SERVICES

OF

LMDS Holdings, Inc.

This Price List contains the descriptions, regulations and rates applicable to the furnishing of local exchange services by LMDS Holdings, Inc. ("LMDS") hereinafter the "Company" with principal offices located at 11111 Sunset Hills Road, Reston, VA 20190. This Price List 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.

CHECK SHEET

Pages of this Price List, as indicated below, are effective as of the date shown at the bottom of the respective pages. Original and revised pages, as named below, comprise all changes from the original Price List and are currently in effect as of the date on the bottom of this page.

PAGE	REVISION		PAGE	REVISION		PAGE	REVISION
Title	Original	*	26	Original	*		
1	Original	*	27	Original	*		
2	Original	*	28	Original	*		
3	Original	*	29	Original	*		
4	Original	*	30	Original	*		
5	Original	*	31	Original	*		
6	Original	*	32	Original	*		
7	Original	*	33	Original	*		
8	Original	*	34	Original	*		
9	Original	*	35	Original	*		
10	Original	*	36	Original	*		
11	Original	*	37	Original	*		
12	Original	*	38	Original	*		
13	Original	*	39	Original	*		
14	Original	*	40	Original	*		
15	Original	*	41	Original	*		
16	Original	*	42	Original	*		
17	Original	*	43	Original	*		
18	Original	*	44	Original	*		
19	Original	*	45	Original	*		
20	Original	*	46	Original	*		
21	Original	*	47	Original	*		
22	Original	*	48	Original	*		
23	Original	*					
24	Original	*					
25	Original	*					

* - indicates those pages included with this filing

TABLE OF CONTENTS

TABLE OF CONTENTS, (CONT'D.)

ALPHABETICAL INDEX

ALPHABETICAL INDEX, CONT'D.)

EXPLANATION OF SYMBOLS

When changes are made in any Price List page, a revised page will be issued canceling the Price List page affected. Changes will be identified on the revised pages(s) through the use of the above mentioned symbols.

The following are the only symbols used for the purposes indicated below:

(D) - Delete Or Discontinue

(I) - Change Resulting In An Increase to A Customer's Bill

(M) - Moved From Another Price List Location

(N) - New

(R) - Change Resulting In A Reduction To A Customer's Bill

(T) - Change in Text or Regulation but No Change In Rate or Charge

PRICE LIST FORMAT

A. **Page Numbering** - Page numbers appear in the upper right corner of the page. Pages are numbered sequentially, however, new pages are occasionally added to the Price List. When a new page is added between pages already in effect, a decimal is added. For example, a new page added between pages 14 and 15 would be 14.1.

B. **Page 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 PSC. For example, the 4th Revised Page 14 cancels the 3rd Revised Page 14. Because of various suspension periods, deferrals, etc, the Florida PSC follows in their Price List approval process, the most current page number on file with the Commission is not always the Price List page in effect. Consult the Check Sheet for the page currently in effect.

C. **Paragraph Numbering Sequence** - There are nine levels of paragraph coding. Each level of coding is subservient to its 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 Price List filing is made with the Florida PSC, an updated Check Sheet accompanies the Price List filing. The Check Sheet lists the pages contained in the Price List, 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. remains the same, just revised revision levels on some pages). The Price List user should refer to the latest Check Sheet to find out if a particular page is the most current on file with the Florida PSC.

SECTION 1 - DEFINITIONS

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

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.

Broadband Wireless Access - Locations from which the Company is providing wireless transmission.

Circuit – A dedicated telecommunications facility provided by the Company to connect two Points of Interconnection as specified by the Customer in a Service Order. Circuits come in different types depending on the speed and data rates provisioned over the physical facilities of the Circuit (i.e., DS1, DS3, OCx, 5 Mbps, 10 Mbps). A Circuit may traverse more than one Link.

Company - LMDS Holdings, Inc., the issuer of this Price List, which is a Nevada corporation, or any of its affiliates which concur in this Price List.

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

Hub – A location used to aggregate multiple services and to interconnect traffic. Transport of information from a Hub to Remotes and vise versa occurs via Links. Transport is provided by line of sight technology which includes point to multipoint and point to point wireless technology.

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 Transport Area (LATA).

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

Link – A direct wireless connection between two physical locations using a single pair of microwave equipment.

SECTION 1 – DEFINITIONS, (CONT'D.)

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

Point of Interconnection – The point at which the Company's responsibility to provide equipment and service ends and the Customer's responsibility for the information begins, as specified in a Service Order.

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

Remote - An end point location which may serve as the termination point for various Circuit types. Transport of information from a Remote to a Hub and vise versa occurs via Links. Transport is provided by line of sight technology which includes point to multipoint or point to point wireless technology. If a site is used as an intermediate location in a chain of point to point services, both ends are defined as a Remote.

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 acceptance by the Company initiates the respective obligations of the parties as set forth therein and pursuant to this Price List.

Site – A location from which radio transmission and reception equipment produces Links within a specific geographical area. A site may be Hub, Remote or Point of Interconnection.

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.

David LaFrance, Regulatory & External Affairs
11111 Sunset Hills Road
Reston, VA 20190

SECTION 1 – DEFINITIONS, (CONT'D.)

United States - The 48 contiguous states and the District of Columbia, Hawaii, Alaska, Puerto Rico, the US 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 Price List, regardless of whether such person or entity is so authorized by the Customer.

SECTION 2 - GENERAL REGULATIONS

2.1 Undertaking of the Company

2.1.1 Scope

The Company undertakes to furnish communications service in connection with one-way and/or two-way information transmission between points within the State of Florida under the terms of this price list.

Customers may use services and facilities provided under this price list to obtain access to services offered by other service providers. The Company is responsible under this price list only for the services and facilities provided herein, and it assumes no responsibility for any service provided by any other entity that purchases access to the Company network in order to originate or terminate its own services, or to communicate with its own Customers.

2.1.2 Shortage of Equipment or Facilities

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 Price List 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.

The provisioning and restoration of services in emergencies shall be in accordance with Part 64, Support D, Appendix A, of the Federal Communications Commission's Rules and Regulations, which specifies the priority system for such activities.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.3 Terms and Conditions

2.1.3.1 Except as otherwise provided herein, service is provided on the basis of a minimum period of at least one month and shall continue to be provided until canceled by the Customer, in writing, on not less than 30 days notice. For the purpose of computing charges in this Price List, a month is considered to have 30 days.

2.1.3.2 Customers may be required to enter into written Service Orders which shall contain or reference the name of the Customer, a specific description of the service ordered, the rates to be charged, the duration of the services, and the terms and conditions in this Price List. Customers will also be required to execute any other documents as may be reasonably requested by the Company.

2.1.3.3 At the expiration of the initial term specified in each Service Order, or in any extension thereof, service shall continue on a month to month basis at the then current rates unless terminated by either party upon 30 days written notice. Any termination shall not relieve the Customer of its obligation to pay any charges incurred under the service order and this Price List prior to termination. The rights and obligations which, by their nature, extend beyond the termination of the term of the service order shall survive such termination.

2.1.3.4 In any action between the parties to enforce any provision of this Price List, the prevailing party shall be entitled to recover its legal fees and court costs from the non-prevailing party in addition to other relief a court may award.

2.1.3.5 This price list shall be interpreted and governed by the laws of the State of Florida without regard of the State's choice of laws provision.

Another telephone company must not interfere with the right of any person or entity to obtain service directly from the Company.

2.1.3.6 Service may be terminated upon written notice to the Customer if:

(a) the Customer is using the service in violation of this Price List, or

(b) the Customer is using the service in violation of the law, or as set forth in Section 2.5.5 of this Price List.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.3 Terms and Conditions, (cont'd.)

2.1.3.7 The Customer agrees to operate Company-provided equipment in accordance with instructions of the Company or its agents. Failure to do so will void Company liability for interruption of service and may make the Customer responsible for damage to equipment pursuant to Section 2.1.3.8 below.

2.1.3.8 The Customer agrees to return to the Company all Company-provided equipment delivered to the Customer within five (5) days of termination of the service in connection with which the equipment was used. Said equipment shall be in the same condition as when delivered to the Customer, except for normal wear and tear.

Customer agrees to reimburse the Company, upon demand, for any reasonable costs incurred by the Company due to the Customer's failure to comply with this provision.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Liability of the Company

2.1.4.1 The liability of the Company for damages arising out of the furnishing of its services, including but not limited to mistakes, omissions, interruptions, delays, errors, or other defects, representations, or use of these services, or arising out of the failure to furnish the service, whether caused by acts of omission, shall be limited to the extension of allowances for interruption as set forth in Section 2.6. The extension of such allowances for interruption shall be the sole remedy of the Customer and the sole liability of the Company. The Company will not be liable for any direct, indirect, incidental, special, consequential, exemplary or punitive damages to Customer as a result of any Company service, equipment or facilities, or the acts, omissions or negligence of the Company's employees or agents.

2.1.4.2 Except for the extension of allowances to the Customer for interruption in service as set forth in Section 2.6, the Company 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, delay, interruption, failure to provide any service or any failure in or breakdown of facilities associated with the service.

2.1.4.3 The Company shall not be liable for any delay or failure of performance or equipment due to causes beyond its control, including but not limited to: acts of God, fire, flood, explosion or other catastrophes; any law, order, regulation, direction, action, or request of the United States Government, or of any other state or local governments having or claiming jurisdiction over the Company, or of any department, agency, commission, bureau, corporation, or other instrumentality of any one or more of these federal, state or local governments, or of any civil or military authority; national emergencies; insurrections; riots; wars; unavailability of rights-of-way or materials; or strikes, lockouts, work stoppages, or other labor difficulties.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Liability of the Company, (cont'd.)

2.1.4.4 The Company shall not be liable for any claims for loss or damages involving any act or omission of (a) any entity furnishing to the Company or to the Company's Customers' facilities or equipment used in conjunction with services or facilities provided by the Company; or (b) common carriers or warehousemen.

2.1.4.5 The Company shall not be liable for any damages or losses due to the fault or negligence of the Customer or due to the failure or malfunction of Customer-provided equipment or facilities.

2.1.4.6 The Customer shall indemnify and hold the Company harmless from any and all loss, claims, demands, suits, or other action, or any liability whatsoever, whether suffered, made, instituted, or asserted by the Customer or any other party or person(s), and for any loss, damage, or destruction of any property, whether owned by the Customer or any other party, caused or claimed to have been caused directly or indirectly by the installation, operation, failure to operate, maintenance, removal, presence, condition, location, or use of any installation so provided. The Company reserves the right to require each Customer to sign an agreement acknowledging acceptance of the provisions of this section as a condition precedent to such installations.

2.1.4.7 The Company is not liable for any defacement of, or damage to, Customer premises resulting from the furnishing of services or equipment on such premises or the installation or removal thereof.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Liability of the Company, (cont'd.)

2.1.4.8 Notwithstanding the Customer's obligations as set forth in Section 2.3 below, the Company shall be indemnified, defended and held harmless by the Customer, or by others authorized by it to use the service, against any claim, loss or damage arising from Customer's use of services furnished under this Price List, including: claims for libel, slander, invasion of privacy or infringement of copyright arising from the material, data, information, or other content transmitted via the Company's service; patent infringement claims arising from combining or connecting the service offered by the Company with apparatus and systems of the Customer or others; and all other claims arising out of any act or omission of the Customer or others, in connection with any service provided by the Company pursuant to this Price List.

2.1.4.9 The entire liability of the Company for any claim, loss, damage or expense from any cause whatsoever shall in no event exceed sums actually paid by Customer for the specific services giving rise to the claim. No action or proceeding against the Company shall be commenced more than thirty (30) days after the date of the occurrence that gave rise to the claim.

2.1.4.10 The Company shall be indemnified and held harmless by the End User against any claim, loss or damage arising from the End User's use of services offered under this Price List including: claims for libel, slander, invasion of privacy or infringement of copyright arising from the End User's own communications; patent infringement claims arising from the End User's combining or connecting the service offered by the Company with facilities or equipment furnished by the End User of another carrier; and all other claims arising out of any act or omission of the End User in connection with any service provided pursuant to this Price List.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Liability of the Company, (cont'd.)

2.1.4.11 The Company does not guarantee or 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 End 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 or by any other party, for any personal injury to, or death of, any person, or persons, or for any loss, damage or destruction of any property, 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, condition, location or use of service furnished by the Company at such locations.

2.1.4.12 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.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Liability of the Company, (cont'd.)

2.1.4.13 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.

2.1.4.14 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.

2.1.5 Notification of Service-Affecting Activities

The Company will provide the Customer reasonable notification of service-affecting activities that may occur. Such activities may include, but are not limited to, equipment or facilities additions, removals or rearrangements and routine preventative maintenance. Generally, such activities are not specific to an individual Customer but affect many Customers' services. No specific advance notification period is applicable to all service activities. The Company will work cooperatively with the Customer to determine the reasonable notification requirements. With some emergency or unplanned service-affecting conditions, such as an outage resulting from cable damage, notification to the Customer may not be possible.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.6 Provision of Equipment and Facilities

2.1.6.1 The Company shall use reasonable efforts to make available services to a Customer on or before a particular date, subject to the provisions of, and compliance by the Customer with, the regulations contained in this Price List. The Company does not guarantee availability by any such date and shall not be liable for any delays in commencing service to any Customer.

2.1.6.2 The Company shall use reasonable efforts to maintain facilities and equipment that it furnishes to the Customer. The Customer may not, nor may the Customer permit others to, rearrange, disconnect, remove, attempt to repair, or otherwise interfere with any of the facilities or equipment installed by the Company, except upon the written consent of the Company.

2.1.6.3 The Company may substitute, change or rearrange any equipment or facility at any time, but shall not thereby alter the technical parameters of the service provided to the Customer.

2.1.6.4 Equipment the Company provides or installs at the Customer Premises for use in connection with the services the Company offers shall not be used for any purpose other than that for which the Company provided it.

2.1.6.5 The Company shall not be responsible for the installation, operation, or maintenance of any Customer-provided communications equipment. Where such equipment is connected to the facilities furnished pursuant to this Price List, the responsibility of the Company shall be limited to the furnishing of facilities offered under this Price List and to the maintenance and operation of such facilities. Subject to this responsibility, the Company shall not be responsible for:

(a) the transmission of signals by Customer-provided equipment or for the quality of, or defects in, such transmission; or

(b) the reception of signals by Customer-provided equipment; or

(c) network control signaling where such signaling is performed by Customer-provided network control signaling equipment.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.7 Special Construction

Subject to the arrangement of the Company and to all of the regulations contained in this Price List, special construction of facilities may be undertaken on a reasonable efforts basis at the request of the Customer. Special construction is that construction undertaken:

(a) where Company facilities are not presently available, and Company agrees to construct those facilities;

(b) of a type other than that which the Company would normally utilize in the furnishing of its services;

(c) over a transmission link 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.

Special Construction may be assesses for point to point to point or point to multipoint radio transmission and reception facilities. Such facilities may include, but are not limited to, radio transmission equipment, transmit and receive antennae, circuit equipment, and professional engineering services fro design and construction of hub and/or remote terminal equipment including mounting of antennae, masts, and installation of transmission cable. Special construction charges will be determined on a case by case basis.

2.1.8 Ownership of Facilities

Title to all facilities provided in accordance with this Price List remains with the Company, its agents, contractors or suppliers.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.9 Non-routine Installation

At the Customer's request, installation and/or maintenance may be performed outside the Company's regular business hours or in hazardous. In such cases, charges based on cost of the actual labor, material, or other costs incurred by or charged to the Company will apply. If installation is started during regular business hours but, at the Customer's request, extends beyond regular business hours into time periods including, but not limited to, weekends, holidays, and/or night hours, additional charges may apply.

2.1.10 Telecommunications Service Priority

The Telecommunications Service Priority System is the regulatory, administrative and operational system authorizing and providing for priority treatment, to provide and restore National Security Emergency Preparedness Telecommunications service. Under the rules of the Telecommunications Service Priority System, The Local Exchange Company is authorized and required to provide and restore services with Telecommunications Service Priority assignments before services without such assignments. The provision and restoration of Telecommunications Service Priority System services shall be in compliance with Part 64, Appendix A, of the Federal Communications Commission's Rules and Regulations, the guidelines set forth in the Telecommunications Service Priority for National Security Emergency Preparedness Service User Manual and Service Vendor Handbook.

2.2 Use of Service

Service is provided for use by the Customer and may be used by others, when so authorized by the Customer, provided that all such usage shall be subject to the provisions of this Price List, and shall not affect the Customer's responsibility for all payments required under this Price List.

2.2.1 Prohibited Uses

2.2.1.1 The services the Company offers shall not be used for any unlawful purpose or for any use for which the Customer has not obtained all required governmental approvals, authorization, licenses, consents and permits.

2.2.1.2 The Company may require a Customer to immediately shut down its transmission if such transmission is causing interference to others.

2.2.1.3 The Customer may not use the services so as to interfere with or impair service over any facilities and associated equipment, or so as to impair the privacy of any communications over such facilities and associated equipment.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.3 Obligations of the Customer

2.3.1 Customer Responsibilities

The Customer shall be responsible for:

(a) the payment of all applicable charges pursuant to this Price List;

(b) damage to or loss of Company facilities or equipment caused by the acts or omissions of the Customer; by the noncompliance by the Customer with these regulations; or by fire or theft or other casualty on the Customer Premises, unless caused by the negligence or willful misconduct of the employees or agents of the Company;

(c) providing at no charge, as specified from time to time by the Company, any needed personnel, equipment, space and power to operate Company facilities and equipment installed on the Customer Premises, and the level of heating and air conditioning necessary to maintain the proper operating environment on such premises;

(d) obtaining, maintaining, and otherwise having full responsibility for all rights-of-way including private or public easements, licenses, roof rights and conduit necessary for the installation and ongoing maintenance of wireless transmission and reception equipment including, but not limited to, roof top antennas, inside wiring and associated indoor equipment used to provide Network Services to the Customer from the Company's designated point of termination or property line to the location of the equipment space described in 2.3.1 (c). Any costs associated with the obtaining and maintaining of the rights-of-way described herein, including the costs of altering the structure to permit installation of Company-provided facilities, shall be borne entirely by, or may be charged by the Company to, the Customer;

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.3 Obligations of the Customer, (Cont'd.)

2.3.1 Customer Responsibilities, (cont'd.)

(e) providing a safe place to work and complying with all federal and state laws and regulations regarding the working conditions on any premises at which Company employees and agents shall be installing or maintaining Company facilities and equipment. The Customer may be required to install and maintain Company facilities and equipment within a hazardous area if, in the Company's opinion, injury or damage to Company employees or property might result from installation or maintenance by the Company. The Customer shall be responsible for identifying, monitoring, removing and disposing of any hazardous material (e.g. friable asbestos) prior to any construction or installation work;

(f) complying with all laws and regulations applicable to, and obtaining all consents, approvals, licenses and permits as may be required with respect to the location of Company facilities and equipment in or on any Customer premises or the right-of-way for which Customer is responsible under section 2.3.1(d); and granting or obtaining permission for Company agents or employees to enter the premises of the Customer at any time for the purpose of installing, inspecting, maintaining, repairing, or upon termination of service as stated herein, removing the facilities or equipment of the Company.

(g) not creating or allowing to be placed or maintained any liens or other encumbrances on the Company's equipment or facilities; and

(h) making Company facilities and equipment available periodically for maintenance purposes at a time agreeable to both the Company and the Customer. No allowance for interruptions in service will be made for the period during which service is interrupted for such purposes.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.3 Obligations of the Customer, (Cont'd.)

2.3.2 Claims

With respect to any service or facilities provided by the Company, the Customer shall indemnify, defend and hold harmless the Company from and against all claims, actions, damages, liabilities, costs and expenses, including reasonable attorney fees for:

(a) any loss, destruction or damage to property of the Company or any third party, or the death or injury to persons, including, but not limited to, employees or invitees of either party, to the extent caused by or resulting from the negligent or intentional act or omission of the Customer, its employees, agents, representatives or invitees; or

(b) any claim, loss, damage, expense or liability for infringement of any copyright, patent, trade secret, or any proprietary or intellectual property right of any third party, arising from any act or omission by the Customer, including, without limitation, use of Company services and facilities in a manner not contemplated by the agreement between Customer and the Company.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.4 Customer Equipment and Channels

2.4.1 In General

A Customer may transmit or receive information or signals via the facilities of the Company.

2.4.2 Station Equipment

2.4.2.1 Customer-provided terminal equipment on the Customer Premises and the electric power consumed by such equipment shall be provided and maintained at the expense of the Customer.

2.4.2.2 The Customer is responsible for ensuring that Customer-provided equipment connected to Company equipment and facilities is compatible with such equipment and facilities. The magnitude and character of the voltages and currents impressed on Company-provided equipment and wiring by the connection, operation, or maintenance of such equipment and wiring shall be such as not to cause damage to the Company-provided equipment and wiring or injury to the Company's employees or to other persons. Any additional protective equipment required to prevent such damage or injury shall be provided by the Company at the Customer's expense.

2.4.3 Interconnection of Facilities

2.4.3.1 Any special interface equipment necessary to achieve compatibility between the facilities and equipment of the Company used for furnishing local exchange service and the channels, facilities, or equipment of others may be provided at the Customer's expense.

2.4.3.2 Local Service may be connected to the services or facilities of other communications carriers only when authorized by, and in accordance with, the terms and conditions of the tariffs, price list or other official rates of the other communications carriers which are applicable to such connections.

2.4.3.3 Facilities furnished under this price list may be connected to Customer provided terminal equipment in accordance with the provisions of this price list.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.4 Customer Equipment and Channels, (Cont'd.)

2.4.4 Inspection and Testing

2.4.4.1 Upon suitable notification to the Customer, and at a reasonable time, the Company may make such tests and inspections as may be necessary to determine that the Customer is complying with the requirements set forth in section 2.4.2.2 for the installation, operation, and maintenance of Customer-provided facilities, equipment, and wiring in the connection of Customer-provided facilities and equipment to Company-owned facilities and equipment.

2.4.4.2 If the protective requirements for Customer-provided equipment are not being complied with, the Company may take such action as it deems necessary to protect its facilities, equipment, and personnel. The Company will notify the Customer promptly if there is any need for further corrective action. Within ten days of receiving this notice the customer must take this corrective action and notify the Company of the action taken. If the Customer fails to do this, the Company may take whatever additional action is deemed necessary, including the suspension of service, to protect its facilities, equipment and personnel from harm. The Company will, upon request 24 hours in advance, provide the Customer with a statement of technical parameters that the Customer's equipment must meet.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.5 Payment Arrangements

2.5.1 Payment for Service

The Customer is responsible for the payment of all charges for facilities and services furnished by the Company to the Customer or to authorized or joint users. For the purposes of this Price List, all rates are in U.S. dollars.

2.5.1.1 Taxes

The Customer is responsible for the payment of any sales, use, gross receipts, excise, access or other local, state and federal taxes, charges or surcharges, however designated (excluding taxes on the Company's net income), imposed on or based upon the provision, sale or use of the Company's services. All such taxes shall be separately designated on the Company's invoices. If an entity other than the Company (e.g., another carrier or a supplier) imposes charges on the Company, in addition to its own internal costs, in connection with a service for which the Company's Non-recurring Charge is specified, those charges will be passed on to the Customer. It shall be the responsibility of the Customer to pay any such taxes that subsequently become applicable retroactively.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.2 Billing and Collection of Charges

The Customer is responsible for the payment of all charges incurred by the Customer or other users for services and facilities furnished to the Customer by the Company.

The Company shall bill on a month-to-month basis all charges incurred by, and credits due to, the Customer under this Price List attributable to services established, provided, or discontinued.

2.5.2.1 Non-recurring charges are due and payable within 30 days after the date an invoice is mailed to the Customer by the Company.

2.5.2.2 The Company shall present invoices for Recurring Charges monthly to the Customer. Recurring charges shall be due and payable within 30 days after the invoice is mailed to the Customer by the Company.

2.5.2.3 When service does not begin on the first day of the month, or end on the last day of the month, the charge for the action of the month in which service was furnished will be calculated on a pro rata basis. For this purpose, every month is considered to have 30 days.

2.5.2.4 Billing of the Customer by the Company will begin on the Service Commencement Date, which is the first day following the date on which the Company notifies the Customer that the service or facility is available for use, except that the Service Commencement Date may be postponed by mutual agreement of the parties, or if the service or facility does not conform to standards set forth in this Price List or the service order. Billing accrues through and includes the day that the service, circuit, arrangement or component is discontinued.

2.5.2.5 If any portion of the payment is received by the Company after the date due, or if any portion of the payment is received by the Company in funds which are not immediately available, then a late payment penalty of 1.5% shall be due to the Company.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.3 Advance Payments

To safeguard its interests, the Company may require a Customer to make an advance payment before services and facilities are furnished. In addition, where special construction is involved, the advance payment may also include an amount equal to the estimated Non-Recurring Charges for the special construction and Recurring Charges (if any) for a period to be set between the Company and the Customer. The advance payment will be credited to the Customer's initial bill. An advance payment may be required in addition to a deposit.

2.5.4 Deposits

The Company does not collect deposits at this time.

2.5.5 Return Check Charge

A. A return check charge of $25.00 will be assessed for checks returned for insufficient funds if the face value of the check does not exceed $50.00.

B. A return check charge of $30.00 will be assessed for checks returned for insufficient funds if the face value of the check exceeds $50.00 but does not exceed $300.00.

C. A return check charge of $40.00 or 5% of the value of the check, whichever is greater, will be assessed for checks returned for insufficient funds if the face value of the check exceeds $300.00.

2.5.6 Disputed Bills

The Customer shall notify the Company of any disputed items on a bill within 30 days of receipt of the bill. If the Customer and the Company are unable to resolve the dispute to their mutual satisfaction, the Customer may file a complaint with the Florida Public Service Commission in accordance with the Commission's rules of procedure.

2.5.6.1 The date of the dispute shall be the date the Company receives sufficient documentation to enable it to investigate the dispute.

2.5.6.2 The date of the resolution is the date the Company completes its investigation and notifies the Customer of the disposition of the dispute.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.5 Discontinuance of Service

2.5.5.1 Upon nonpayment of any amount owing the Company, the Company may, by giving ten (10) days prior written notice to the Customer, discontinue or suspend service without incurring any liability.

2.5.5.2 Upon violation of any of the other material terms or conditions for furnishing service, the Company may, by giving 30 days prior written notice to the Customer, discontinue or suspend service without incurring any liability if such violation continues during that period.

2.5.5.3 Upon condemnation of any material portion of the facilities used by the Company or its agents to provide service to a Customer or if a casualty renders all or any material portion of such facilities inoperable beyond feasible repair, the Company, by notice to the Customer, may discontinue or suspend service without incurring any liability.

2.5.5.4 Upon the Customer's insolvency, assignment for the benefit of creditors, filing for bankruptcy or reorganization, or failing to discharge an involuntary petition within the time permitted by law, the Company may immediately discontinue or suspend service without incurring any liability.

2.5.5.5 Upon any governmental prohibition or required alteration of the services to be provided or any violation of an applicable law or regulation, the Company may immediately discontinue service without incurring any liability.

2.5.5.6 Upon the Company's discontinuance of service to the Customer under Section 2.5.5.1 or 2.5.5.2, the Company, in addition to all other remedies that may be available to the Company by law or in equity or under any other provision of this Price List, may declare all future monthly and other charges which would have been payable by the Customer during the remainder of the term for which such services would have otherwise been provided to the Customer to be immediately due and payable.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.5 Discontinuance of Service, (cont'd.)

2.5.5.7 Immediately and without notice, if the Company deems 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 sub-section 2.5.5.7 if

(a) the Customer refuses to furnish information to the Company regarding the Customer's credit-worthiness, its past or current use of Common Carrier communications services or its planned use of service(s);

(b) the Customer provides false information to the Company regarding the Customer's identity, address, credit-worthiness, past or current use of Common Carrier communications services, or its planned use of the Company's service(s);

(c) the Customer states that it will not comply with, or fails to comply with, a request of the Company for security for the payment for service(s) in accordance with Section 2.5.4;

(d) 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 other Common Carrier communications services to which the Customer either subscribes or had subscribed or used;

(e) the Customer uses service to transmit a message, locate a person or otherwise give or obtain information without payment for the service;

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.5 Discontinuance of Service, (cont'd.)

2.5.5.7 (continued)

(f) the Customer uses, or attempts to use, service with the intent to avoid the payment, either in whole or in part, of the Price Listed charges for the service by:

(1) using or attempting to use service by rearranging, tampering with, or making connections to the Company's service not authorized by this Price List;
(2) using tricks, schemes, false credit devices, electronic devices; or
(3) any other fraudulent means or devices;

(g) the Customer owes any sum thirty (30) days past due;

(h) within five (5) working days of the date of written notice to the Customer that the Customer is not complying with any provision of this Price List, the noncompliance is not corrected.

2.5.5.8 The discontinuance of service(s) by the Company pursuant to this Section 2.5.5 does not relieve the Customer of any obligation to pay the Company for charges due and owing for service(s) furnished up to the time of discontinuance.

2.5.5.9 Upon the Company's discontinuance of service to the Customer under Section 2.5.6.1 or 2.5.6.2, all applicable charges, including but not limited to termination charges, reasonable attorneys' fees, or any other fees incurred by the Company in the collection of any amount due under this price list for services rendered or facilities provided, shall become due. Any attorneys' or other collection fees incurred by the Company after discontinuance of service shall become due immediately upon invoice of such fees to the customer. This is in addition to all other remedies that may be available to the Company at law or in equity or under any other provision of this price list.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.6 Cancellation of Application for Service

2.5.6.1 Applications for service cannot be canceled unless the Company otherwise agrees. Where the Company permits Customer to cancel an application for service prior to the start of service or prior to any special construction, no charges will be imposed except for those specified below.

2.5.6.2 Where, prior to cancellation by the Customer, the Company incurs any expenses in installing the service or in preparing to install the service that it otherwise would not have incurred, a charge equal to the costs the Company incurred, less net salvage, shall apply. In such case, the charge will be based on such elements as the cost of the equipment, facilities, and material, the cost of installation, engineering, labor, and supervision, general and administrative expense, other disbursements, depreciation, maintenance, taxes, provision for return on investment, and any other costs associated with the construction or arrangements.

The special charges described in 2.5.6.2 will be calculated and applied on a case-by-case-basis.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.6 Allowances for Interruptions in Service

Interruptions in service, which are not due to the negligence of, or noncompliance with the provisions of this Price List by, the Customer or the operation or malfunction of the facilities, power or equipment provided by the Customer, will be credited to the Customer as set forth in 2.6.1 for the part of the service that the interruption affects.

2.6.1 Credit for Interruptions

2.6.1.1 A credit allowance will be made when an interruption occurs because of a failure of any component furnished by the Company under this Price List. An interruption period begins when a Customer reports a service, facility or circuit is interrupted and releases it for testing and repair. An interruption period ends when the service, facility or circuit is repaired or is inoperative but the Customer declines to release it for testing and repair.

2.6.1.2 For calculating credit allowances, every month is considered to have 30 days. A credit allowance is applied on a pro rata basis against the rates specified thereunder and is dependent upon the length of the interruption. Only those facilities on the interrupted portion of the circuit will receive a credit.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.6 Allowances for Interruptions in Service

2.6.1 Credit for Interruptions, (cont'd.)

2.6.1.3 A credit allowance will be given for interruptions of 15 minutes or more. Credit allowances will be calculated as follows:

Interruptions of 24 hours or Less:

Length of Period to be Credited	**Interruption Credit**
Less than 15 minutes	None
15 minutes up to, but not including 3 hours	1/10 Day
3 hours up to, but not including 6 hours	1/5 Day
6 hours up to, but not including 9 hours	2/5 Day
9 hours up to, but not including 12 hours	3/5 Day
12 hours up to, but not including 15 hours	4/5 Day
15 hours up to, but not including 24 hours	One Day

Two or more interruptions of 15 minutes or more during any 24-hour period shall be considered as one interruption.

Interruptions Over 24 Hours and Less Than 72 Hours. Interruptions over 24 hours and less than 72 hours will be credited 1/5 day for each 3-hour period or fraction thereof. No more than one full day's credit will be allowed for any period of 24 hours.

Interruptions Over 72 Hours. Interruptions over 72 hours will be credited 2 days for each full 24-hour period. No more than 30 days credited will be allowed for any one month period.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.6 Allowances for Interruptions in Service, (Cont'd.)

2.6.2 Limitations on Allowances

No credit allowance will be made for:

(a) interruptions due to the negligence of, or noncompliance with the provisions of this Price List by, the Customer, authorized user, joint user, or other common carrier providing service connected to the service of the Company;

(b) interruptions due to the negligence of any person other than the Company, including but not limited to the Customer or other common carriers connected to the Company's facilities;

(c) interruptions due to the failure or malfunction of non-Company equipment;

(d) interruptions of service during any period in which the Company is not given full and free access to its facilities and equipment for the purpose of investigating and correcting interruptions;

(e) interruptions of service during a period in which the Customer continues to use the service on an impaired basis;

(f) interruptions of service during any period when the Customer has released service to the Company for maintenance purposes or for implementation of a Customer order for a change in service arrangements;

(g) interruption of service due to circumstances or causes beyond the control of the Company;

(h) interruptions of service not reported to the Company within thirty (30) days of the date that service was affected.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.6 Allowances for Interruptions in Service, (Cont'd.)

2.6.3 Use of an Alternative Service

Should the Customer elect to use another means of communications during the period of interruption, the Customer must pay the charges for the alternative service used.

2.6.4 Cancellation For Service Interruption

Cancellation or termination for service interruption is permitted only if any circuit experiences a single continuous outage of 8 hours or more or cumulative service credits equaling 16 hours in a continuous 12-month period. The right to cancel service under this provision applies only to the single circuit which has been subject to the outage or cumulative service credits.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.7 Cancellation of Service

If a Customer cancels a Service Order or terminates services before the completion of the term for any reason whatsoever other than a service interruption (as defined in 2.6.1 above), Customer agrees to pay to Company the following sums which shall become due and owing as of the effective date of the cancellation or termination and shall be payable within the period set forth in 2.5.2: 1) all Non-Recurring charges reasonably expended by the Company to establish service to Customer, plus 2) any disconnection, early cancellation or termination charges reasonably incurred and paid to third parties by the Company on behalf of Customer, plus 3) all Recurring Charges specified in the applicable Service Order for the balance of the then current term.

2.8 Transfers and Assignments

Neither the Company nor the Customer may assign or transfer its rights or duties in connection with the services and facilities provided by the Company without the written consent of the other party, except that the Company may assign its rights and duties (a) to any subsidiary, parent company or affiliate of the Company; (b) pursuant to any sale or transfer of substantially all the assets of the Company; or (c) pursuant to any financing, merger or reorganization of the Company.

SECTION 2 - GENERAL REGULATIONS, (CONT'D.)

2.9 Notices and Communications

2.9.1 The Customer shall designate on the Service Order an address to which the Company shall mail or deliver all notices and other communications, except that Customer may also designate a separate address to which the Company's bills for service shall be mailed.

2.9.2 The Company shall designate on the Service Order an address to which the Customer shall mail or deliver all notices and other communications, except that Company may designate a separate address on each bill for service to which the Customer shall mail payment on that bill.

2.9.3 Except as otherwise provided in Section 2.3.2, all notices or other communications required to be given pursuant to this Price List will be in writing. Notices and other communications of either party, and all bills mailed by the Company, shall be presumed to have been delivered to the other party on the third business day following placement of the notice, communication or bill with the U.S. Mail or a private delivery service, prepaid and properly addressed, or when actually received or refused by the addressee, whichever occurs first.

2.9.4 The Company or the Customer shall advise the other party of any changes to the addresses designated for notices, other communications or billing, by following the procedures for giving notice set forth in Section 2.9.3.

2.10 Hearing and Speech Impaired Persons

Intrastate toll message rates for TDD users shall be evening rates for daytime calls and night rates for evening and night calls.

2.11 Telecommunications Relay Service

For intrastate toll calls received from the relay service, the Company will when billing relay calls discount relay services calls by 50 percent off of the otherwise applicable rate for a voice no relay call except that were either the calling or called party indicates that either party is both hearing and visually impaired, the call shall be discounted 60 percent off of the otherwise applicable rate for a voice no relay call. The above discounts apply only to time-sensitive elements of a charge for the call and shall not apply to per call charges such as a credit card surcharge.

SECTION 3 - SERVICE DESCRIPTIONS

3.1 Broadband Wireless Service

3.1.1 Description of Service

Broadband Wireless service is offered as a high capacity dedicated transmission facility available 24 hours per day, 7 days per week. Customers may commit to one, two or three year service terms. The minimum service period for Broadband Wireless services is one year. Should the Customer terminate service prior to the end of the term commitment, the Customer will be billed a termination charge equal to the monthly recurring charge times the number of months remaining in the term.

Broadband Wireless services is an intrastate interexchange service that provides dedicated wireless bandwidth between a Customer designated premises and a Company Point of Presence (POP). Dedicated wireless bandwidth is provisioned from a Company base station to a location selected by the Customer. The base station transmits and the hub equipment receives a point-to-point or point-to-multipoint transmission utilizing radio frequencies in the Local Multipoint Distribution Service (LMDS 27.5 to 31.225 GHz) spectrum. The entire usable bandwidth of the transmission path is available and dedicated to the Customer for their exclusive use. LMDS frequencies provide line-of-sight transmission and will not penetrate trees, walls, glass or other path-obstructing materials. The use of time-division multiple access (TDMA) and FDMA (frequency DMA) technology allows multiple customers within a 3-7 mile coverage radius to share the same radio channel (multipoint).

SECTION 3 - SERVICE DESCRIPTIONS, (CONT'D.)

3.1 Broadband Wireless Service, (Cont'd.)

3.1.2 Limitations

Service will be provided subject to availability and where technical capabilities permit. The following limitations will apply to the provision of all Broadband Wireless services.

Broadband Wireless microwave equipment requires an unobstructed line-of-sight to a point of interconnection with the Company's base station. Actual data transmission rates depend on a number of factors, including, but not limited to the distance from the customer selected receive site to the Broadband Wireless transmission point. The customer shall be responsible for any and all costs associated with obtaining and maintaining rights-of-way at a receiver site, including costs of altering a structure to permit installation of Company provided facilities. Customer shall bear all such costs which will be charged by the Company subject to Customer's prior approval. The Company may require the Customer to demonstrate compliance with this section prior to accepting an order for service.

Service is offered subject to the availability of necessary facilities or equipment, or both facilities and equipment, and subject to the provisions of this Price List. The obligation of Broadband Wireless to provide service is dependant upon its ability to procure, construct, and maintain facilities that are required to meet the customer's order for service. Broadband Wireless' provision of service through its own facilities requires the use of microwave transmit/receive equipment. The receive equipment must be attached to or located upon the customer's location, often on the roof of the building in which the customer premises is located. Broadband Wireless equipment cannot be installed on the rooftop without the consent of the building owner and/or property manager(s). In addition, Broadband Wireless equipment cannot be installed without access to the building's telephone closet(s), which may not be under the control of the customer or Broadband Wireless. Therefore, Broadband Wireless facilities-based services are subject to the availability of rooftop access and telephone closet access. Broadband Wireless will make all reasonable efforts to secure the necessary facilities.

SECTION 3 - SERVICE DESCRIPTIONS, (CONT'D.)

3.1 Broadband Wireless Service, (Cont'd.)

3.1.2 Limitations, (cont'd.)

Broadband Wireless reserves the right to limit or to allocate the use of existing facilities when necessary due to lack of facilities, relevant resources, or causes beyond the Company's control.

Broadband Wireless does not undertake to transmit messages, but offers the use of its facilities when available, and will not be liable for errors in transmission nor for failure to establish connections.

The Customer shall ensure that its equipment and/or system is properly interfaced with Broadband Wireless facilities or services; that the signals emitted into Broadband Wireless network are of the proper mode, bandwidth, power, signal level or other technical parameters for the intended use of the Customer and in compliance with the criteria set forth in this Price List, and that the signals do not damage equipment, injure personnel or degrade service to other Customers.

SECTION 3 - SERVICE DESCRIPTIONS, (CONT'D.)

3.1 Broadband Wireless Service, (Cont'd.)

3.1.3 Wireless T-1

Wireless T-1 is a Broadband Wireless managed service offering providing Customer a total turnkey transport product including: installation; 24 hour/7 day a week network monitoring, maintenance and network performance reporting; detailed billing; and, on-going post-sales support. A Customer purchases connectivity between a Company wireless base station and a remote hub site of its choosing. The Broadband Wireless customer can purchase fixed bandwidth on a single wireless sector on a PTP or PTMP basis in the following increments:

- 4 T-1s
- 6 T-1's
- 8 T-'s
- 10 T-1's
- 12 T-1's

3.1.4 Wireless Ethernet

Wireless Ethernet utilizes Broadband Wireless technology to deliver Layer-2, 10/100BaseT or faster metropolitan Ethernet connections or Dedicated Internet Access (DIA). The Wireless Ethernet product can be used to deliver end-to-end wireless connectivity utilizing standardized 10Mbps or 100Mbps Ethernet interfaces. Wireless Ethernet services can be configured as oversubscribed and unprotected if required by Broadband Wireless customers. Customers can oversubscribe the fixed amount of bandwidth sold/allocated at any rate up to the fixed amount of bandwidth sold/allocated and use the allocated bandwidth for any purpose. The Broadband Wireless customer can purchase fixed bandwidth on a single wireless sector on a point to point or point to multipoint basis in the following increments:

Wireless Ethernet	**Dedicated Internet Access**
5 Mbps	5 Mbps
10 Mbps	10 Mbps
15 Mbps	20 Mbps
20 Mbps	

SECTION 3 - SERVICE DESCRIPTIONS, (CONT'D.)

3.1 Broadband Wireless Service, (Cont'd.)

3.1.5 Rates and Charges

Rates and charges for Broadband Wireless services are specified below. The Customer will be billed a fixed, flat Monthly Recurring Charge (MRC) for bandwidth in addition to a Non-Recurring Charge (NRC) for installation services provided at the same customer location. Additional Federal, State and Local taxes and Surcharges may also apply. Rates indicated below do not include sales, use, gross receipts, excise, access or other local, state and federal taxes, charges, user fees, or surcharges.

A. Rate Elements

1. **Air Link.** - A monthly recurring Air Link rate element provides for the dedicated transmission media between a customer designated premise and the Company's Point of Presence. One Air Link charge applies for each transmission path and per each customer point of termination.

2. **Port Charge** - A monthly recurring Port Charge rate element applies for each Wireless T1 or Wireless Ethernet port access connection to the Broadband Wireless network. The specified charge is billed per port per month for the dedicated bandwidth increments specified below.The monthly recurring Port Charge is based on the Committed Constant Bit Rate specified in the Service Agreement between Broadband Wireless and Customer. Data rates for Customer Ethernet traffic may not exceed the dedicated bandwidth set out in the Service Agreement. Burst charges may apply where Customer exceeds the Committed Constant Bit Rate specified in the Service Agreement

SECTION 3 - SERVICE DESCRIPTIONS, (CONT'D.)

3.2 Terrestrial DS1 Service

Terrestrial DS1 Service is a dedicated, high capacity, full duplex channel with a line speed of 1.544 Mbps isochronous serial data having signal format of either Alternate Mark Inversion (AMI) or Bipolar 8 Zero Substitution (B8ZS) and either Super frame (D4) or Extended Super frame formats. DS1 Service has the equivalent capacity of 24 Voice Grade services or 24 DS0 services. AMI can support 24 56Kpbs channels and B8ZS can support 24 64Kbps channels.

SECTION 4- RATES AND CHARGES

4.1 Broadband Wireless Service

4.1.1 Wireless T1 Rates

	Monthly Recurring Charges		Non Recurring Charges	
	Air Link	**Port**	**Air Link**	**Port**
4 T-1s	$300	$120	$1,500	$1,500
6 T-1's	$450	$180	$1,500	$1,500
8 T-'s	$600	$240	$1,500	$1,500
10 T-1's	$750	$300	$1,500	$1,500
12 T-1's	$890	$360	$1,500	$1,500

4.1.2 Wireless Ethernet Rates

	Monthly Recurring Charges		Non Recurring Charges	
	Air Link	**Port**	**Air Link**	**Port**
5 Mbps	$400	$200	$750	$750
10 Mbps	$525	$200	$750	$750
15 Mbps	$850	$200	$750	$750
20 Mbps	$1,600	$200	$750	$750

4.1.3 Dedicated Internet Access Rates

	Monthly Recurring Charges		Non Recurring Charges	
	Air Link	**Port**	**Air Link**	**Port**
5 Mbps	$775	$200	$750	$750
10 Mbps	$1,300	$200	$750	$750
20 Mbps	$2,050	$200	$750	$750

SECTION 4- RATES AND CHARGES, (CONT'D.)

4.2 Terrestrial DS1 Service

Terrestrial DS1 voice loop monthly recurring charge	ICB
Terrestrial DS1 voice loop install charge	ICB