

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K/A

(Mark One)

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

For the Fiscal Year Ended December 31, 2000

OR

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

For the Transition Period from to

Commission File Number 1-15343

Williams Communications Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

73-1462856
(I.R.S. Employer Identification No.)

One Williams Center, Tulsa, Oklahoma
(Address of principal executive offices)

74172
(Zip Code)

Registrant's Telephone Number, Including Area Code:
(918) 573-2000

Securities Registered Pursuant to Section 12(b) of the Act:

<u>Title of Each Class</u>	<u>Name of Each Exchange on Which Registered</u>
Class A Common Stock, \$0.01 par value, and Preferred Stock Purchase Rights	New York Stock Exchange

Securities Registered Pursuant to Section 12(g) of the Act:
6.75% Redeemable Cumulative Convertible Preferred Stock

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 Regulation 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.

The aggregate market value of the registrant's Class A common stock held by nonaffiliates as of the close of business on February 28, 2001, was approximately \$1.2 billion. In addition, the aggregate market value of the registrant's Class B common stock held by The Williams Companies, Inc. as of the close of business on February 28, 2001, was approximately \$4.9 billion.

The number of shares of the registrant's Class A Common Stock outstanding at February 28, 2001, was 92,859,410.

DOCUMENTS INCORPORATED BY REFERENCE

Not applicable.

WILLIAMS COMMUNICATIONS GROUP, INC.

FORM 10-K

PART I

Item 1. Business

(a) General Development of Business

Williams Communications Group, Inc. (WCG) was incorporated under the laws of the State of Delaware on December 1, 1994, under the name of WilTel Technology Ventures, Inc. The name of the corporation was changed to The WilTech Group, Inc. on September 20, 1995, and to Williams Communications Group, Inc. on February 11, 1997.

In 1985, The Williams Companies, Inc. (Williams) entered the communications business by pioneering the placement of fiber-optic cables in pipelines no longer in use. Williams also pioneered the strategy of providing services solely to other communications providers. By 1989, through a combination of construction projects and acquisitions, Williams had completed the fourth nationwide digital fiber-optic network, consisting of approximately 9,700 miles. By 1994, WilTel, Williams' communications subsidiary, was one of the top four providers of high capacity data services, one of the top five providers of long distance voice services, and the first provider to offer nationwide frame relay transmission capacity. In January 1995, Williams sold the WilTel network business to LDDS Communications (now WorldCom). Williams excluded from the sale an approximately 9,700 route mile single fiber network comprised of a single fiber-optic strand and associated equipment along the original nationwide network, WilTel's telecommunications equipment distribution business and Vyvx Services. In January 1998, Williams reentered the communications network business, announcing its plans to develop the Williams network.

Until the closing of the initial public offering of a minority interest in WCG stock on October 6, 1999, WCG was a wholly owned subsidiary of Williams. In its initial public offering, WCG offered for sale 29,600,000 shares of its Class A common stock to the public. The underwriters for the initial public offering, Salomon Smith Barney Inc., Lehman Brothers Inc. and Merrill Lynch & Co., exercised their options and purchased 4,440,000 additional shares to cover over-allotments. In separate private placements, SBC Communications Inc., Intel Corporation, and Teléfonos de México, S.A. de C.V., respectively, acquired 20,226,812, 9,225,093 and 4,612,546 shares of WCG's Class A common stock.

Williams owns 100 percent of WCG's outstanding Class B common stock, which gives Williams approximately 98 percent of the voting power of WCG. In addition, on February 26, 2001, Williams and WCG entered into an agreement under which Williams transferred assets to WCG in exchange for 24,265,892 shares of WCG's Class A Common Stock. Williams owns approximately 86 percent of the total outstanding Class A and Class B common stock of WCG. As a majority-owned subsidiary of Williams, WCG has in place with Williams agreements for the provision of certain administrative and other services, for the lease of certain property and facilities, for the sharing of tax liabilities and benefits, and for the license of the Williams name and logo.

Williams has announced that its board of directors has authorized its management to take steps that may lead to a tax-free distribution of shares of WCG's common stock held by Williams to its shareholders. Assuming that market conditions and other factors continue to support such a tax-free spin-off, Williams has announced that its board of directors would expect to vote during the first part of 2001 to set a record date, the ratio of a share of WCG stock that will be issued for each share of Williams stock, and to direct the distribution of WCG shares.

On January 29, 2001, WCG announced that it had reached an agreement with Platinum Equity, LLC to sell its Houston-based enterprise services operating segment, Williams Communications Solutions (Solutions). Under the terms of the Sale and Purchase Agreement by and among Williams Communications, LLC, Williams Learning Network, Inc., Williams Communications Solutions, LLC, Platinum Equity, LLC, WCS Acquisition Corporation, and WCS Acquisition LLC, Platinum Equity will acquire Solutions' operations in the United States and Mexico as well as the Canadian professional services operations of Solutions. WCG will retain the right to collect Solutions' receivables aged over ninety days at the time of the closing, and Platinum Equity will act as the collection agent for these receivables. WCG also announced its intent to sell the remaining Canadian operations of Solutions in 2001.

The principal executive offices of WCG are located at One Williams Center, Tulsa, Oklahoma 74172 (telephone (918) 573-2000).

(b) Financial Information About Segments

See Part II, Item 8 — Financial Statements and Supplementary Data.

(c) Narrative Description of Business

Substantially all operations of WCG are conducted through subsidiaries. The term "WCG" also includes the operating subsidiaries where the context requires. WCG's principal sources of cash are from external financings, public debt, and public equity. WCG may also receive dividends and advances from its subsidiaries, investments, payments by subsidiaries for services rendered, and interest payments from subsidiaries on cash advances. The amount of dividends available to WCG from subsidiaries largely depends upon each subsidiary's earnings and operating capital requirements and contractual restrictions in each subsidiary's credit arrangements.

Following its decision to sell its Solutions segment, WCG operates through three operating segments: Network, Broadband Media, and Strategic Investments. Network owns or leases and operates a nationwide inter-city fiber-optic network, which it is extending locally and globally to provide Internet, data, voice and video services exclusively to communications service providers. Network also includes a publicly traded Australian telecommunications company and various other investments that drive bandwidth usage on the WCG network. Broadband Media includes Vyvx® Services which provides live and non-live video transmission services worldwide for news, sports, advertising and entertainment events and investments in domestic broadband media communication companies. Strategic Investments invests in both domestic and foreign companies that it believes will, directly or indirectly, increase revenue opportunities for its other segments. As of December 31, 2000, Strategic Investments' foreign investments are all located in South America. WCG has formed strategic alliances with communications companies to secure long-term, high-capacity commitments for traffic on its network and to enhance its service offerings. The Solutions segment has been treated as discontinued operations. Item 1(c) of this report is formatted to reflect the continuing operations of the business.

NETWORK

WCG owns or leases and operates a nationwide inter-city fiber-optic network, which it is extending locally and globally. It intends to make Network the most efficient U.S.-based provider of advanced Internet, data, voice, and video services to companies that use high-capacity communications services as an integral part of their service offerings. These companies include long distance carriers, local service providers, Internet service providers, application service providers, digital subscriber line service providers, utilities, and international carriers. WCG also offers rights of use in dark fiber, which is fiber that it installs but for which it does not provide communications

transmission services. Network is building networks, or seeking strategic relationships to provide services, in U.S. cities and in Asia, Australia, South America, and Europe. Network has also made investments in companies that assist it in improving, or create demand for capacity on, its network. Based on currently announced plans, WCG's global network will include ownership interests in or rights to use:

- in excess of 41,000 miles of fiber-optic cable currently completed, connecting 125 U.S. cities;
- fiber-optic cable networks within 50 of the largest U.S. cities;
- approximately 150 data centers located in 125 U.S. cities;
- 15,000 miles of dark fiber in Europe connecting the UK, France, Switzerland, Italy, Austria, Germany, Belgium, the Netherlands, Norway, Denmark, Finland, and Sweden;
- operational border crossings between the U.S. and Mexico in California and Texas; and
- in excess of 250 STM-1 equivalent circuits on 7 major undersea cable systems connecting the U.S. with Europe, Asia, and Australia.

Revenues

Network contributed approximately the following percentages to WCG's total revenues for the past three years:

<u>Percentage of Total Revenues</u>	<u>Year</u>
84	2000
73	1999
55	1998

Strategy

Network's objective is to be the most efficient U.S.-based provider of advanced high capacity Internet, data, voice, and video services to national and international communications service providers. To achieve this objective, it intends to:

- *Become the leading provider to communications carriers.* WCG's focus is on providing high-quality communications services to carriers as they seek to benefit from the growth in communications demand. It also offers its customers the flexibility to control their own service platforms so that they choose to buy services from WCG rather than build these capabilities themselves or purchase them from another carrier. WCG's focus on selling wholesale services to carriers works to its advantage because its customers do not see it as a competitive threat in the retail market.
- *Deploy a technologically advanced network.* WCG is combining advanced optical and electronic transmission and switching equipment with its innovative network design to offer highly flexible, efficient, and reliable network services to its customers. Its innovative network design provides high-quality network services to support voice, data, Internet, and video traffic at a lower investment than other currently deployed network architectures due to the elimination of several layers of costly equipment. WCG's research investment and technological position has enabled the creation of a multi-protocol/multi-service architecture supporting the full array of DWDM, SONET, ATM, and IP services. This multi-service platform positions WCG as a unique migration partner for incumbent through next generation service providers.

- *Expand local access services.* WCG is installing or otherwise acquiring interests in fiber-optic cable or other facilities within 50 of the largest U.S. cities. It is installing high-speed synchronous optical network (SONET) transport and dense wave division multiplexing (DWDM) equipment to offer a broad range of high-capacity or broadband services. This expansion will enable it to extend the high-capacity services of its network to virtually every major carrier hotel, network peering point, and managed content site within those cities. Enhancing the level of connectivity directly to these strategic targets re-enforces commercial relationships with customers by minimizing churn, reducing the time to deliver existing services, and using advanced technologies to promote new service creation to its customers.
- *Enhanced Internet Protocol (IP) Services.* WCG is installing 16 core carrier class IP router sites connected to key peering, managed content, and switching access points. This additional capability enables it to provide next generation products as an Internet infrastructure service provider to support emerging voice, data, Internet, and video service requirements.
- *Establish global connectivity.* WCG has or is pursuing ownership interests in, or rights to capacity on, various undersea and foreign fiber-optic cables. These cables will connect its U.S. network to Europe, South America, Asia, and Australia. Additionally, WCG pursues strategic relationships that (i) allow it to exchange dark fiber and/or capacity on its network for cost-effective access, dark fiber, and/or capacity on international networks or (ii) allow it to use its network construction and management experience to construct or manage international networks. WCG also intends to establish alliances with international carriers that will expand its capabilities throughout Europe and other key markets.
- *Pursue strategic alliances.* In order to increase revenues and decrease unit costs, WCG pursues strategic alliances with communications providers that offer the potential for long-term, high-capacity commitments for traffic on its network. To date, WCG has entered into strategic alliances with SBC, Intel, Teléfonos de México, KDDI, Winstar, and others to provide network services. Strategic alliances also allow it to combine its capabilities with those of its alliance partners in order to offer its customers a more complete product set, including local and international capacity and Internet access services.
- *Invest in technology and communications companies.* WCG invests in and works with companies that increase its access to new technologies that can result in substantial increases in the capacity, accessibility, or efficiency of its network. WCG also invests in companies that can facilitate its ability to offer complementary products or services to its customers.
- *Become a leader in bandwidth trading.* WCG has taken an approach to bandwidth trading that incorporates risk management strategies and portfolio management practices. WCG perceives its asset infrastructure, customer base, and market position as portfolios that can be leveraged to maximize value and mitigate risk. WCG is the only company participating in this industry that manages its network pricing function within its trading group.

Properties

U.S. Inter-City Network

In late 2000, Network substantially completed its U.S. inter-city core network build, which connects 125 cities. The following table describes the U.S. inter-city network infrastructure (numbers are approximate):

<u>The WCG Network</u>	<u>Planned Route Miles</u>	<u>Miles in Operation</u>	<u>Average Number of Fibers</u>	<u>Average Number of Fibers Retained*</u>	<u>Average Number of Spare Conduits</u>
U.S. Inter-City					
Single fiber network(1) . . .	14,400	9,700	1	1	N/A
Other wholly owned fiber builds	13,100	5,400	106	28	1.8
Fiber builds under Asset Defeasance Program	5,000	5,000	127	24	1.9
Fiber builds jointly owned(2)	1,300	1,300	43	12	0
Routes through dark fiber rights(3)	<u>7,900</u>	<u>6,600</u>	13	10	0.3
Total	<u>41,700</u>	<u>28,000</u>			

<u>Local Network</u>	<u>Planned</u>	<u>Completed</u>
Local builds in number of cities	50	14

* This is the average number of fibers in each category that Network expects to retain for its own use and not grant rights in dark fiber to others.

- (1) As part of the agreements relating to the sale of the WilTel network business to LDDS (now WorldCom) in January 1995, Williams retained a 9,700-mile single fiber network. In 1998, WCG entered into an agreement with WorldCom whereby it received an option to purchase one fiber-optic strand over approximately 7,700 miles of selected WorldCom routes. WCG has exercised its right to purchase 4,700 miles of these routes. The single fiber network, and all fiber-optic strands it purchases pursuant to the option, may be used only to transmit video or multimedia services, including Internet services, until July 1, 2001. After this date, these fiber-optic strands may be used for any purpose, including voice and data services.
- (2) This category consists of Network's fiber rights in builds which have been jointly constructed, or rights in dark fiber obtained by WCG, Enron Communications, Inc., and Touch America, Inc. through a limited liability company, or LLC, in which WCG shares equal ownership and control. The LLC constructed the portion of the route between Portland and Las Vegas and obtained rights in dark fiber in the portion of the route between Las Vegas and Los Angeles and in the Detroit-Cleveland route. The LLC owns the right of way over some of the route it constructed, with each of WCG, Enron, and Touch America also contributing rights of way. The LLC granted rights in dark fibers on the completed routes to each of WCG, Enron, Touch America, and others. Network provides operational services to the LLC.
- (3) This category consists of rights in dark fiber and conduits that Network has obtained or intends to obtain. Network has already obtained approximately 7,900 route miles, all of which have had fiber-optic cable installed. Network manages the transmission equipment on the routes it acquired, and it typically pays for the maintenance of fiber-optic strands and rights of way.

Network is currently installing new transmission equipment on its single fiber network to increase its transmission capacity and ensure its compatibility with the newer portions of the network. Due to advances in transmission electronics, it is now possible to carry as much traffic on this single fiber-optic strand as on 128 fiber-optic strands four years ago. In addition, the single fiber network will provide additional routes for the network into select major markets.

Network leases capacity from both long distance and local telecommunications carriers, including its competitors, in order to meet the needs of its customers. Leases of capacity are distinguished from rights in dark fiber in that capacity leases are for only a portion of the fiber capacity and the lessor supplies and operates the equipment to transmit over the fiber. Capacity leases are generally for terms of one month up to five years, but can be longer. Network leases approximately 15 percent of its network capacity currently in use. However, because it has more capacity available on its network than it is currently using, the leased capacity it currently uses constitutes approximately eight percent of the total capacity currently available on the network. These leases are for areas where Network does not have on-network portions, or its on-network is not currently sufficient to meet the expected capacity. This includes capacity to provide service from Network's facility to another provider's facility. These leases of capacity may contain minimum commitments that Network will make in order to obtain better pricing. In some cases, Network must obtain service from other carriers at costs that exceed its revenues for providing the required service. In doing so, it attempts to balance its off-network commitments with the expected requirements of its customers.

In September 2000, Network acquired the long distance network assets of Ameritech Communications, Inc., a subsidiary of SBC. The assets acquired are located in the states of Illinois, Indiana, Michigan, Ohio, and Wisconsin, and include a 2,000-mile fiber-optic network over four routes, indefeasible rights of use in dark fiber, and 15 data centers.

City-by-city buildout. The following table sets forth Network's current and future plans for its network build.

<u>Fiber Build Segment</u>	<u>Estimated Completion Date</u>	<u>Approximate Route Miles</u>	<u>Approximate Operational Miles</u>
Albany - Boston	Complete	183	183
Atlanta - Jacksonville ⁽¹⁾	Complete	355	355
China Cable: Bandon Connections	Complete	293	293
Daytona - Orlando - Tampa	Complete	153	153
Dallas - Houston ⁽²⁾	Complete	250	250
Denver - Salt Lake City ⁽¹⁾	Complete	551	551
Detroit - Cleveland ⁽²⁾	Complete	172	172
Herndon, VA - Wash. D.C. - New York City ⁽¹⁾	Complete	377	377
Houston - Atlanta - Washington ⁽¹⁾	Complete	1,825	1,825
Houston - McAllen - Laredo - San Antonio ⁽²⁾	Complete	705	705
Jacksonville - Miami ⁽¹⁾	Complete	332	322
Kansas City - Denver ⁽¹⁾	Complete	635	635
L.A. - NYC ⁽²⁾	Complete	4,370	4,370
LA - Phoenix - San Antonio - Austin - Houston	Complete	1,994	1,394
LA - Sacramento - Oakland - San Jose ⁽³⁾	Complete	804	762
LA - San Diego ⁽²⁾	Complete	150	150
Miami - Tampa - Tallahassee ⁽¹⁾	Complete	540	540
Minneapolis - Kansas City ⁽¹⁾	Complete	452	452
New Orleans - Tallahassee	Complete	471	471
Portland - Salt Lake City - LA ⁽⁴⁾	Complete	1,316	1,316
SUSA - NEW ⁽²⁾⁽⁵⁾	Complete	4,700	0

<u>Fiber Build Segment</u>	<u>Estimated Completion Date</u>	<u>Approximate Route Miles</u>	<u>Approximate Operational Miles</u>
SUSA - OLD ⁽²⁾⁽⁵⁾	Complete	9,700	9,700
ACI ⁽⁶⁾	1Q 2001	1,997	0
Atlanta - Nashville - Cincinnati - Indianapolis - Chicago	1Q 2001	985	0
Cleveland - New York City	1Q 2001	748	0
Houston - Kansas City - St. Louis - Chicago	1Q 2001	1,452	812
New York - Boston (2 diverse routes) ⁽⁷⁾	1Q 2001	562	294
Salt Lake City - Sacramento - San Francisco - Santa Clara	1Q 2001	911	911
Chicago - Cleveland - Pittsburg - Harrisburg - Wash. D.C.	2Q 2001	882	0
China Cable San Luis Obispo/Manchester Connections	2Q 2001	654	289
Denver - Amarillo - Wichita Falls - Dallas ⁽²⁾	2Q 2001	750	0
Minneapolis - Milwaukee - Chicago - Detroit ⁽⁷⁾	2Q 2001	1,239	431
Portland - Seattle ⁽⁷⁾	2Q 2001	369	191
Sacramento - Portland ⁽³⁾	2Q 2001	688	150
TAT 14 Cable Tuckerton, N.J. - Manasquan, N.J. - New York City Connections	2Q 2001	155	0

- (1) These routes have been constructed under Network's asset defeasance program.
- (2) Network has rights in dark fiber with no spare conduits along these routes.
- (3) Network has obtained rights in 12 dark fibers on these routes along with two spare conduits. It will install, wholly own, and operate a fiber-optic cable within one of these conduits.
- (4) These routes were jointly constructed or obtained by WCG, Enron, and Touch America with no spare conduits.
- (5) As part of the agreements relating to the sale of the WorldCom network business to LDDS (now WorldCom) in January 1995, Williams retained a 9,700-mile single fiber network. In 1998, WCG entered into an agreement with WorldCom whereby it received an option to purchase one fiber-optic strand over approximately 7,700 miles of selected WorldCom routes. WCG has exercised its right to purchase 4,700 miles of these routes. The single fiber network, and all fiber-optic strands it purchases pursuant to the option, may be used only to transmit video or multimedia services, including Internet services, until July 1, 2001. After this date, these fiber-optic strands may be used for any purpose, including voice and data services.
- (6) In September 2000, Network acquired the long distance network assets of Ameritech Communications, Inc., a subsidiary of SBC. The assets acquired are located in the states of Illinois, Indiana, Michigan, Ohio, and Wisconsin, and include a 2,000-mile fiber-optic network over four routes, indefeasible rights of use in dark fiber, and 15 data centers.
- (7) In addition to constructing one route with two spare conduits, Network has obtained rights in 12 dark fibers along a different route between these cities.

Network design and technology. Network is combining advanced optical and electronic transmission equipment with its innovative network design to offer more flexible and efficient network services to its customers. Some characteristics of the network that it is constructing are as follows:

- *Multi-service platform.* A multi-service operating system allows Internet, data, voice and video services to be provided on a single asynchronous transfer mode, or ATM, operating system. Most other carriers use multiple platforms, or operating systems, which create distinct networks and organizations for each service provided. Due to its unified platform approach, Network hopes to achieve greater efficiency and lower costs.

- *ATM core switching.* ATM core switching is a packet switching and transmission technology based on sending various types of information, including voice, data, and video, in fixed-sized cells. Packet-based networks transport information compressed as "packets" over circuits shared simultaneously by several users. Newly developed equipment based on advanced communications standards enables packet-based networks to carry voice and data more efficiently, with greater predictability and at a lower cost than other networks.
- *Internet protocol network.* Network has upgraded its Internet protocol, or IP, network to operate substantially at OC-48 capacity over SONET technology.
- *Advanced fiber-optic cable.* Newer fiber-optic cable, including Corning's Enhanced LEAF™ fiber and Lucent's TruWave™ fiber, has a wider range of spectrum than previously deployed fibers over which to send wavelengths of light, enabling a greater number of wavelengths to be sent over long distances.
- *DWDM.* Dense wave division multiplexing is a technology that allows transmission of multiple waves of light over a single fiber-optic strand, thereby increasing network capacity. By using DWDM, Network is able to derive 80 bi-directional wavelengths, at OC-192 capacity per wavelength, which is a capacity of 10 gigabits per second, over a single fiber-optic strand with current technology. Network expects this equipment to increase capacity per fiber by 250 percent over the existing technology, while reducing the cost of transmission.
- *Use of optically meshed SONET instead of SONET rings.* The use of optically meshed SONET allows every location on the WCG network to be connected to multiple locations. Optically meshed SONET provides for more recovery options in the case of a network failure, permits rapid provisioning of customer services, and allows for full utilization of capacity. Most other networks use SONET rings, which automatically reverse signals at a specific point along a network in the event of a network failure, providing for only one recovery option. A SONET ring design also requires installation of up to twice as much capacity for the same amount of traffic as compared to Network's optically meshed SONET design.
- *Closer spacing of transmission electronics.* Network's spacing of transmission electronics at 40-mile intervals allows it to take advantage of the latest advances in DWDM and other advances in optical technology by reducing the distance over which light has to travel. Most other fiber networks space their electronics at 60-mile intervals.
- *Elimination of digital cross-connect system.* The ATM packet technologies that Network employs eliminate the need for a high-cost, high-maintenance digital cross-connect system. Circuit-based systems are the predecessor to the ATM packet technologies Network employs. The elimination of unnecessary equipment also reduces Network's operating and maintenance expenses.
- *Nortel DMS 250 switches.* Network uses the latest Nortel switching technology to efficiently carry traditional voice services on its ATM core network. Nortel DMS 250 voice switches have been installed in the metropolitan areas of Anaheim, San Francisco, Kansas City, Houston, Boston, Atlanta, Newark, Chicago (Broadview), and San Antonio. Network intends to install switches in the Dallas metropolitan area in 2001.

Data centers. As of December 31, 2000, Network had 146 data centers across its network. Data centers are environmentally controlled, secure sites designed to house transmission, routing and switching equipment, and local operational staff, as well as space and power for colocation customers. By collocating their own equipment in Network's facilities, customers are able to minimize the use of expensive local loops from local telephone companies to reach Network's

backbone. The customer also foregoes the capital and operating expense required to build and maintain its own data centers. By expanding its network to include multiple data centers within select major metropolitan areas, Network will provide an end-to-end solution for its carrier customers.

Conduit and fiber-optic cable. The newer portions of the WCG network are designed for expandability and flexibility and will contain multiple conduits along approximately 70 percent of its routes. To construct its fiber-optic cable, fiber-optic strands are placed inside small plastic tubes and bundles of these tubes are wrapped with plastic and strengthened with metal. Network then places these bundles inside the conduit, which is high-density polyethylene hollow tubing 1½ to 2 inches in diameter. The conduit is generally buried approximately 42 inches underground along pipeline or other rights of way. Network also uses steel casing in high-risk areas, including railroad crossings and high-population areas, thereby providing for greater protection. The first conduit contains a cable generally housing between 96 and 144 fibers, and the second conduit, or third where constructed, serves as a spare. The spare conduits allow for future technology upgrades, potential conduit sales, and expansion of capacity at costs significantly below the cost of new construction. After existing and anticipated leases of dark fiber, Network generally plans to retain approximately 24 fibers for its own use on the constructed portions of its network.

Rights of way. The WCG network is primarily constructed by digging trenches along rights of way, or rights to use the property of others, which Network obtains throughout the United States from various landowners. Where feasible, Network constructs along Williams' pipeline rights of way and the rights of way of other pipeline companies. WCG believes that use of pipeline rights of way gives its network inherent advantages over other systems built over more public rights of way, such as railroads, highways, telephone poles, or overhead power transmission lines. These advantages include greater physical protection of the fiber system and lower construction costs. Approximately 21 percent of its rights of way are along Williams' pipeline rights of way and the remainder is along the rights of way of third parties. Rights of way from unaffiliated parties are generally for terms of at least 20 years, and most cover distances of less than one mile. Where necessary or economically preferable, Network has other right of way agreements in place with highway commissions, utilities, political subdivisions and others. Almost all of its rights of way extend through at least 2018.

Monitoring. Network monitors its network 24 hours a day, seven days a week, from its network management centers in Tulsa, Oklahoma, and St. Louis, Missouri. Each network management center provides centralized network surveillance, troubleshooting, and customer service. The system currently allows technicians to detect a component malfunction in the WCG network, quickly reroute the customer's traffic to an available alternate path, and effect an expedited repair. Network expects this will reduce service costs and customer downtime. It has also implemented a program that encourages people to phone a toll-free number prior to breaking ground, backed up by its "call before you dig" group to reduce the risk of damage to its conduit or fiber system. Additionally, Network places above ground markers at frequent intervals along the route of its network.

Local Network Expansion

In 2000, WCG announced plans to spend \$421 million to extend the local reach of its network. It intends to have in operation local services over its network in 50 of the largest U.S. cities by December 31, 2003. As of December 31, 2000, it had in operation local services over its network in 14 U.S. cities and intends to have in operation local services over its network to a total of 20 of the largest U.S. cities by December 31, 2001. Network will add fiber and computer equipment to extend the high capacity services of its nationwide inter-city network to virtually every major carrier hotel and network peering point within those cities. It expects construction to complete this year in six

cities, including San Diego, Salt Lake, Minneapolis, Baltimore, Santa Clara, and Miami. In addition to the local network builds that it will perform, Network will use 86,000 local fiber miles over 3,200 route miles that it obtained in a fiber swap with Metromedia Fiber Network. It expects this to provide it with connections to an additional 250 points of presence in 18 cities. Currently, Network has accepted significant builds completed in Boston, Chicago, Dallas, New York, Philadelphia, San Francisco, Washington, D.C., Houston, and Los Angeles.

Network will utilize wireless local loops obtained from Winstar. Currently Network has accepted 72 hubs in 40 cities. It is also pursuing interconnection agreements with certain local service providers to obtain, among other things, access to unbundled network elements that it can use to provide enhanced local services to its customers.

Global Network Expansion

Europe. WCG has 20-year reciprocal buy/sell agreements with Telia, the national communications service provider in Sweden, pursuant to which it will receive rights to use dark fiber on Telia's planned 28,000-mile fiber-optic network in Europe. Network has the ability to accept between two and 36 fiber strands, depending on the route, across Telia's network. This network is scheduled to connect approximately 35 of the largest European cities, with completion scheduled by the end of 2001. Telia's network will consist of existing fiber, fiber currently being installed, and fiber leased from others.

Australia. PowerTel, Ltd. has built, owns, and operates communications networks connecting and serving the three Australian cities of Brisbane, Melbourne, and Sydney with long distance and local services in the central business districts of these cities. Each of the three Australian utilities serving these cities has entered into a 20-year agreement with PowerTel that allows PowerTel to use the utilities' ducts and to lay fiber-optic cable alongside their rights of way between the cities. PowerTel's strategy is to provide high-quality, low-cost local voice, data, and Internet services to the commercial and carrier markets. WCG's total investment currently represents a 45 percent economic interest in PowerTel. WCG consolidates PowerTel's results of operations with its own because it is entitled to appoint a majority of the members of PowerTel's board of directors, and thereby exercises control over its operations.

China-U.S. cable and Japan-U.S. cable. WCG acquired SBC's interests in these two cables in June 2000. One interconnection point for the China-U.S. cable is fully operational, and the second is expected to be operational by the end of first quarter. The China-U.S. cable is a 16,000-mile loop system, with capacity of 80 gigabits per second. The Japan-U.S. cable will operate initially at 80 gigabits per second, and eventually, the cable can be expanded to 640 gigabits per second. The Japan-U.S. cable is scheduled to become fully operational by the end of the third quarter of 2001.

Asia-Pacific Cable Network (APCN-2). A consortium of carriers is building APCN-2, an intra-Asia 11,500-mile undersea cable project that will connect China, Hong Kong, Japan, South Korea, Malaysia, the Philippines, Singapore, and Taiwan. As an initial participant in the network build, WCG will acquire significant capacity on APCN-2, which is scheduled to be in operation by first quarter 2002. The cable will operate initially at 80 gigabits per second and can be expanded to 2,560 gigabits per second. APCN-2 will intersect with the China-U.S. and Japan-U.S. cables described above.

TAT-14 cable system. Under an agreement with Telia, the national communications service provider in Sweden, WCG obtained additional capacity on the TAT-14 cable system, which connects the United States with the United Kingdom, The Netherlands, Denmark, Germany, and France. TAT-14 is scheduled to become operational by the end of second quarter of 2001 and will operate at 640 gigabits per second.

Southern Cross Cable Network. WCG acquired capacity on this network in April 2000. Southern Cross is an undersea cable network linking Australia and New Zealand with Hawaii and the West Coast of the United States. This cable was completed in November 2000 and operates at 200 gigabits per second.

Products and Services

Network's products and services fall into seven categories:

- packet-based data services
- private line services
- voice services
- optical wave services
- dark fiber and conduit rights
- colocation and hosting services
- network design and operational support.

Packet-based data services. These services provide efficient connectivity for Internet, data, voice, and video networks at variable capacities to connect two or more points. Specific packet-based data services include ATM, frame relay, and Internet transport services. These services are provided over the WCG network and enable it to bill based on service features and usage. In addition, Network intends to introduce new services such as virtual private network, wholesale dial, and wholesale digital subscriber line services over its network.

Private line services. Network provides customers with fixed amounts of point-to-point capacity. These services are billed on fixed monthly fees, regardless of usage.

Voice services. Network has deployed voice-switching capability, allowing customers to originate and terminate long distance traffic. In addition, it has entered into service agreements with a number of other domestic and international carriers ensuring complete service beyond the cities served directly by its network. Network currently offers its customers wholesale origination, termination, and complete long distance services, as well as calling card, directory assistance, operator assistance, international, and toll-free services.

Optical wave services. In November 1999, WCG became one of the first communications providers to begin offering optical wave services to customers. These services allow a customer exclusive long-term use of a portion of the transmission capacity of a fiber-optic strand rather than the entire fiber strand. The capacity it uses to provide optical wave services is in addition to the capacity used by it to provide its other services. Network is able to derive from a single fiber strand with existing technology up to 320 bi-directional wavelengths, at OC-48 capacity per wavelength. A purchaser of optical wave services installs its own electrical interface, switching, and routing equipment. Optical wave services allow a customer to purchase capacity in smaller increments while retaining the control advantages of dark fiber.

Dark fiber and conduit rights. Network sells rights to use dark fiber and related services. In addition, from time to time, it sells rights to conduit and installs conduit for its customers. Purchasers of dark fiber rights typically install their own electrical and optical transmission equipment. Substantially all of its current and planned builds include laying two spare conduits, and Network may sell rights to use at least one of them. A purchaser of conduit rights typically lays its own cable inside the conduit. Related services for both sales of rights for dark fiber and conduits include colocation of customer equipment at Network's data centers and other network equipment

locations and maintenance of the purchased fiber or conduit. Payment for dark fiber rights is generally made at the time of delivery and acceptance of the fiber, although other payment options may be available. In addition, ongoing payments for maintenance services are required.

Colocation and hosting services. Network provides its customers with access to and space in its data centers to install their own equipment necessary to connect to the WCG network. WCG believes that providing colocation services on its network increases the sales of its other services by attracting Internet and applications service providers. Its colocation services offer potential customers reduced costs for capacity, reduced expenses compared to building and operating their own facilities, rapid turn-up of circuits for additional capacity, interconnection with its network and other networks, and improved network performance.

WCG also intends to provide hosting services, which include web sites on the Internet, and storage of, and access to, data and other media content. This will be provided on large computer servers owned by Network and located in its data centers that can be used by its customers on a dedicated or shared basis.

Network design and operational support. Network helps its customers design and operate their networks. It uses its network management centers to monitor and operate portions of their networks. Network is deploying new management tools, including its customer network management system, which will give its customers the ability to monitor network performance and reconfigure their capacity from their own network management centers on an essentially real-time basis and the ability to increase or reduce bandwidth rapidly to better match their needs. This customer network management system features equipment inventory management, bandwidth inventory management, configuration management, fault isolation management, and alarm monitoring.

Customers

Network's customers currently include regional Bell operating companies, Internet service providers, application service providers, digital subscriber line service providers, long distance carriers, utilities, international carriers, and other communications services providers who desire high-speed connectivity on a carrier services basis. Sales to SBC accounted for 24 percent of Network's 2000 revenues; sales to Intermedia, including its subsidiary, Digex Incorporated, accounted for 19 percent of Network's 2000 revenues; and sales to Winstar accounted for 14 percent of its 2000 revenues. In September 2000, WorldCom announced an agreement to purchase Intermedia.

WCG has entered into strategic alliances with SBC, Intel, Teléfonos de México, KDDI, Winstar, and others. It also has investments in Lightyear, XO Communications, and UtiliCom and communications companies with operations in Australia, Brazil, Chile, and Argentina. These alliances and investments help to increase the volume of business and provide additional customers for Network. WCG anticipates that over the next several years the distribution of its revenues will shift in part as a result of increased usage of its services by the companies with whom it has entered into strategic alliances. WCG does not believe these alliances and investments will adversely impact its relationships with its other customers. For more information about these strategic alliances, see the section of entitled "Strategic Alliances" below.

Sales and Marketing

Network's sales and marketing department is small and focused, resulting in strong customer relationships and lower operating costs. This organization consists of senior level management personnel and experienced sales representatives with extensive knowledge of the industry and Network's products and key contacts within the industry at various levels in the carrier organizations.

Competition

The communications industry is highly competitive. Some competitors in the markets of carrier services and fiber-optic network providers may have personnel, financial, and other competitive advantages. In the market for carrier services, Network competes primarily with the three traditional nationwide carriers, AT&T, WorldCom, and Sprint, and other coast-to-coast and regional fiber-optic network providers, such as Qwest, Level 3, Global Crossing and Broadwing. Other companies have announced plans to construct significant fiber-optic networks. Network also competes with numerous other service providers that focus either on a specific product or set of products or within a geographic region. Network competes primarily on the basis of pricing, transmission quality, network reliability, and customer service and support. Network has only recently begun to offer some of its services and products and, as a result, it may have fewer and less well established customer relationships than some of its competitors. Its services within local markets in the United States face additional competitors, including the regional telephone companies and other local telephone companies. Its services outside the United States also face additional competitors, including national telephone companies in foreign countries and carriers that own capacity on other submarine and regional fiber-optic systems.

Some of Network's competitors are expanding capacity on their existing networks or developing new networks. The prices Network charges its customers for transmission capacity on its network could decline due to installation by Network and its competitors of fiber and related equipment that provides substantially more transmission capacity than currently needed. If prices for network services decline, WCG may experience a decline in revenues that would have a material adverse effect on its operations.

Investments

WCG believes that its investments in and work with technology companies in their development stages facilitates improvements in its network through the rapid adoption and deployment of those technologies that offer the ability to lower costs and substantially increase transmission speeds. WCG also invests in companies that can facilitate its ability to offer complementary products or services to its customers. It also invests in communications companies in order to solidify commercial relationships, which may increase business on the WCG network. WCG has investments, none of which exceed five percent of outstanding common stock, in several public companies, including the following:

Accelerated Networks. Accelerated Networks, Inc. focuses on developing integrated access devices. Their products support network carriers in efficiently connecting many different types of customer services ranging from Internet access, voice over Internet protocol, corporate remote access, virtual private networks, and telephone service.

Avici Systems. Avici Systems, Inc. is a manufacturer of terabit routers.

Corvis. Corvis Corporation is a manufacturer of long-haul optical transmission equipment.

GoConnect. GoConnect is an Australian-based Internet media company with a core business focused on interactive video advertising using proprietary technology with free Internet service to gain an audience.

ONI Systems. ONI Systems is a manufacturer of optical networking DWDM systems for local service providers.

Sonus Networks. Sonus Networks is a manufacturer of advanced open services switch equipment, including equipment that delivers voice over Internet protocol services.

TMNG. The Management Network Group, Inc. is a provider of strategic, management, operational, and e-business consulting services to the telecommunications industry.

XO Communications. XO Communications, Inc. provides a variety of high-quality telecommunications services and high-speed Internet access to business customers. WCG acquired these shares of XO Communications through a recent merger of Concentric Network Corporation with XO Communications. WCG previously owned shares of Concentric, which were converted into XO Communications Class A common stock in the merger.

WCG also has investments in several private companies, including Amber Networks, Inc.; Charlotte's Networks, Inc.; Epoch Internet; Hostcentric, Inc.; ipVerse, Inc.; Lightyear Communications, Inc.; Mahi Networks, Inc.; MariTEL; Telica, Inc.; Tenor Networks, Inc.; UtiliCom Networks, LLC; and Zaffire, Inc.

BROADBAND MEDIA

In first quarter of 2000, WCG formed its Broadband Media segment. Substantially all of the operations of this segment are conducted by Vyvx Services. Since 1989, Vyvx Services has provided worldwide transmission of live and non-live media content, transmitting broadcast news, sports, advertising, and special events over its integrated fiber-optic, satellite, and teleport network. Vyvx Services serves the unique video needs of major broadcast networks and their affiliate stations, professional sports leagues, media production companies, and global advertising agencies. Vyvx Services transmits approximately 80 percent of live major league sporting events, approximately 65 percent of live events and distributes approximately 35 percent of spot advertising. Through Vyvx Services, WCG has gained experience in broadband multimedia networks and established high-speed connections to major news and sports venues throughout the United States. WCG provides services throughout the United States, South America, and Asia using its network, four satellite earth stations that it owns, and leased transmission capacity on satellites. WCG owns approximately 600 servers that are located in television and radio stations throughout the United States, which allow for online, real-time selection and distribution of media content. Broadband Media also has investments in companies that provide media content products and services.

Revenues

Broadband Media contributed approximately the following percentages to WCG's total revenues for the past three years:

<u>Percentage of Total Revenues</u>	<u>Year</u>
20	2000
27	1999
43	1998

Products and Services

Broadband Media's primary products and services fall into two primary categories:

- video transmission services, which include broadcast quality transmission of live and non-live video content for the news, entertainment and sports markets;
- media distribution services, which include distribution of video and audio spot advertisements and programs to television and radio stations.

Strategy

Broadband Media's objective is to provide a wide variety of media-centric products and services primarily to the media and entertainment industries, which drives traffic on the WCG network. WCG intends to use its long-standing customer relationships to provide high-quality communications services to broadcast networks, cinematic production houses, and other carriers as they seek to benefit from the growing demand for high capacity media and entertainment products and services. In addition, WCG is initiating implementation of an application infrastructure called MediaXtranetSM that will provide services to facilitate the transmission and storage of media content for business-to-business applications, including hosting and navigation services. WCG expects that MediaXtranet would enable the collection, gathering, hosting, management, transacting, and edge distribution of media content, regardless of its format or source. WCG expects that the full implementation of MediaXtranet, if undertaken, would likely require substantial capital expenditures, which are currently not accounted for in its business plan.

If undertaken in full, WCG would intend to utilize MediaXtranet to capitalize on its broadband media experience and existing customer relationships to expand its products and services to include the following:

- media and entertainment content logging, storage, and portal-type access and distribution
- media streaming for both audio and video services
- optical distribution of cinematic and television broadcasts and advertisements
- media and entertainment eCommerce transactional activities
- Internet-based distribution of advertisements

Customers

Broadband Media sells only to media content service providers. It does not compete with its media customers for retail end-users. It has approximately 2,000 customers, including major broadcast and cable television networks, news services, professional and collegiate sports organizations, such as the National Football League and the National Basketball Association, and advertising agencies, television companies, and movie production companies. Approximately 43 percent of Broadband Media's total revenue in 2000 was derived from its top 10 customers. Broadband Media's largest customer, Fox Entertainment Group, Inc., accounted for approximately 13 percent of Broadband Media's 2000 total revenues. Contracts with the largest customers are for terms that extend up to 10 years. Most contracts with smaller customers are for one-year terms.

Sales and Marketing

Broadband Media has 50 sales personnel located in offices in 12 cities throughout the United States. Its office in Miami serves markets in South America. It also has an office in Singapore that serves markets in Asia. Thirty-nine of its sales people are focused on selling to those

customers who use video and media transmission services and 11 of its sales people are focused on selling to those customers who use advertising distribution services.

Competition

Vyvx Services is currently a market leader in transmission services for major league and other sporting and live events and has a significant market share of the advertising distribution services market. Competitors in traditional video transmission and advertising distribution services include Teleglobe, Triumph Communications, Inc., and Digital Generation Systems, Inc.

Investments

WCG believes that investing in companies that are developing new products and services utilizing broadband media technology will help it better serve its customers. Its investments include the following businesses:

ChoiceSeat™. CSI, Inc. deploys ChoiceSeat touch-screen display units installed on stadium seats that provide access to statistics, different camera angles, player- and venue-related information, and access to current information from other sports events. WCG owns 100 percent of the outstanding common stock and 28 percent of the outstanding preferred stock of CSI, which together represent slightly less than a 50 percent economic and voting interest in CSI. Other investors in CSI include Intel, Microsoft Corporation and Axalon (Offshore) I, L.P.

Others. Broadband Media has also made investments in other domestic companies, including SporTVision Systems, Inc., Xstream Sports, Inc. and Pinnacle Systems, Inc.

STRATEGIC INVESTMENTS

Through Strategic Investments, WCG invests in communications businesses that it believes will increase revenue opportunities for the WCG network and other business segments. The strategic investments currently include ownership interests in the following communications companies located in Brazil, Chile, and Argentina:

ATL-Algar Telecom Leste S.A. ATL was formed in March 1998 to acquire the concession for B-band cellular licenses in the Brazilian states of Rio de Janeiro and Espirito Santo. As of December 31, 2000, WCG owned 19 percent of the outstanding common stock and 66 percent of the outstanding preferred stock of ATL through WCG's ownership of Johi Representacoes Limitada and Williams International ATL Ltd. Other investors in ATL include SBC, Algar Telecom, S.A. and Teléfonos de México.

In the first quarter of 2001, WCG granted an option to Telecom Américas, Ltd., a joint venture among SBC, American Movil S.A. de C.V., and Bell Canada International Inc., under which WCG granted an option to purchase WCG's remaining interest in ATL for an agreed to price. The option was granted in exchange for Telecom Américas paying WCG's portion of a required funding to ATL. The option will expire at the end of first quarter 2001.

ATL provides digital cellular services in the Brazilian states of Rio de Janeiro and Espirito Santo, covering a population of approximately 16.1 million inhabitants. ATL started commercial operations on January 15, 1999, and had approximately 1.62 million subscribers as of December 31, 2000. ATL's only cellular competitor in these areas is Tele Sudeste Celular Participacoes S.A., a former subsidiary of Telebras currently controlled by a consortium led by Telefonica de Espana. During first quarter of 2001, Brazil intends to auction three additional frequency bands, which will result in increased competition early in year 2002. Even with increased competition, WCG believes the Rio concession to remain an attractive alternative due to its large established customer base, the

low expected churn to new entrants and its proven high-quality, 100 percent digital cellular network, offering a broad range of enhanced services, strong name recognition and excellent customer service.

Manquehue Net. Manquehue Net, S.A. (formerly Telefonica Manquehue, S.A.) is a high-capacity communications services provider within the Santiago, Chile, metropolitan area. It provides Internet, data and voice services for its approximately 75,000 business and residential customers as of December 31, 2000. Manquehue Net was formed as a result of the merger of Metrocom S.A. with Telefonica Manquehue in January 2000. Manquehue Net is installing an extensive telecommunications duct infrastructure throughout Santiago, which had exceeded more than 250,000 homes and businesses by the end of 2000. WCG owned a 19.9 percent equity interest in Metrocom S.A. until the merger. As a result of the merger and subsequent investments by WCG and other shareholders, WCG now owns 16.5 percent of Manquehue Net.

Silica Networks. In May 2000, WCG acquired a 19.9 percent direct interest in Silica Networks S.A. (formerly Southern Cone Communications Company, S.A.). Manquehue Net also acquired a 30.1 percent interest in Silica Networks. The 4,300-kilometer (2,660-mile) Silica Networks' network initially will link the major Argentine cities of Buenos Aires, Las Toninas, Rosario, Cordoba, Mendoza, and Neuquen with the Chilean cities of Santiago and Valparaiso. When complete, the system will link Argentina and Chile with cables to Peru, Colombia, Panama, Venezuela, Brazil, and the Caribbean, and ultimately to the WCG U.S. network.

Revenues

Strategic Investments contributed approximately the following percentages to WCG's total revenues for the past three years:

<u>Percentage of Total Revenues</u>	<u>Year</u>
— *	2000
6	1999
14	1998

* Beginning in 2000, Strategic Investments consisted only of investments in businesses accounted for either on an equity or cost basis.

STRATEGIC ALLIANCES AND RELATIONSHIPS

WCG enters into strategic alliances with communications companies to secure long-term, high-capacity commitments for traffic on the WCG network and to enhance its service offerings. It currently has strategic relationships with SBC, Intel, Teléfonos de México, KDDI, and Winstar. WCG intends to continue to pursue additional strategic alliances.

WCG has entered into, and will continue to enter into, strategic alliances and strategic relationships with communications companies to secure long-term, high-capacity commitments for traffic on the WCG network and to enhance its service offerings. The most significant of these alliances are described below.

SBC Communications Inc. SBC is a major communications provider in the United States. SBC currently provides local services in the south central and Midwest regions of the United States and in California, Nevada, and Connecticut. Concurrently with the WCG initial public offering, on October 6, 1999, SBC acquired 20,226,812 shares of WCG Class A common stock, which represents approximately 4.1 percent of the shares of capital stock outstanding as of February 28,

2001. In connection with its purchase of this common stock at the time of the initial public offering, SBC agreed to certain restrictions and will receive certain privileges, including the following:

- SBC has a right to acquire additional shares of WCG Class A common stock which cannot exceed a total ownership interest of 10 percent of all classes of WCG common stock outstanding on a combined basis until at least 2009.
- SBC has agreed not to transfer to anyone except affiliates any of its shares of WCG common stock until April 2003, unless WCG has a change of control.
- SBC has the right to nominate a member of the WCG board of directors at such time as SBC has more than a 5 percent equity interest in WCG and is allowed to offer long distance services in a state in its traditional exchange service area. Although SBC currently is not entitled to exercise this right, a director designated by SBC has been elected to, and is currently a member of, the WCG board of directors.
- SBC has a right to maintain its equity interest in the WCG common stock, which will be forfeited if SBC fails to exercise this right twice. Following a second failure to exercise, SBC has a right to maintain its newly diluted position so long as it maintains at least a 3 percent equity interest.
- SBC has the right to require WCG to register under the Securities Act its shares of WCG Class A common stock.

WCG has an option to purchase all the shares of Class A common stock acquired by SBC in the event of the termination of certain agreements with SBC. Williams, so long as it has a 50 percent equity interest in WCG, has a right of first purchase with respect to any shares of WCG common stock that SBC should decide to offer. WCG has a right of first purchase with respect to any shares not purchased by Williams.

WCG has entered into agreements with SBC that provide that:

- Until 2019, SBC must first seek to obtain from WCG domestic voice and data long distance services and select international wholesale services.
- Until 2019, WCG must first seek to obtain from SBC select international wholesale services and various other services, including switched voice services such as toll-free, operator, calling card, and directory assistance services.
- SBC and WCG will sell each other's products to their respective customers and provide installation and maintenance of communications equipment and other services.

For the services each must seek to obtain from the other, the prices generally will be equal to the cost of the product or service plus a specified rate of return. However, these prices cannot be higher than prices charged to other customers and in some circumstances cannot be higher than specific rates. If either party can secure lower prices for comparable services that the other party will not match, then that party is free to utilize the lowest cost provider.

Both WCG and SBC can provide services or products to other persons. Each party may also sell or utilize the products or services purchased from the other to provide products or services to other persons. However, if SBC establishes a wholesale distribution channel to resell the network capacity purchased from WCG to another provider of carrier services, WCG has the right to increase the price it charges SBC for the services SBC resells in this manner. While the terms of these agreements with SBC are intended to comply with restrictions on SBC's provision of long distance services, various aspects of these arrangements have not been tested under the Telecommunications Act.

WCG and SBC have agreed to a mechanism for the development of projects that would allow the interconnection of the SBC network with the WCG network based on the unanimous decision of committees composed of an equal number of representatives from WCG and SBC. If a committee does not approve a project, both WCG and SBC have the right, subject to certain exceptions, to require the other party to develop a project in exchange for payment of the direct costs and cost of capital required to complete the project or pursue it on its own. In addition, upon SBC receiving authorization from the FCC to provide long distance services in any state in its traditional telephone exchange service region, SBC has the option to purchase from WCG at net book value all voice or data switching assets that are physically located in that state and of which SBC has been the primary user. The option must be exercised within one year of the receipt of authorization. WCG then has one year after SBC's exercise of the option to migrate traffic, install replacement assets, and complete other transition activities. This purchase option would not permit SBC to acquire any rights of way that WCG uses for its network or other transport facilities that it maintains. Upon termination of the alliance agreements with SBC, SBC has the right in certain circumstances to purchase voice or data switching assets, including transport facilities, of which SBC's usage represents 75 percent or more of the total usage of these assets.

SBC may terminate the provider agreements if any of the following occurs:

- WCG begins to offer retail long distance voice transport or local exchange services on its network except in limited circumstances
- WCG materially breached its agreements with SBC causing a material adverse effect on the commercial value of the relationship to SBC
- WCG has a change of control without SBC's consent
- SBC acquires an entity that owns a nationwide fiber-optic network in the United States and determines not to sell long distance assets to WCG

WCG may terminate the provider agreements if any of the following occurs:

- SBC has a change of control
- there is a material breach by SBC of the agreements, causing a material adverse effect on the commercial value of the relationship to WCG

Either party may terminate a particular provider agreement if the action or failure to act of any regulatory authority materially frustrates or hinders the purpose of that agreement. There is no monetary remedy for such a termination.

In the event of termination due to its actions, WCG could be required to pay SBC's transition costs of up to \$200 million. Similarly, in the event of termination due to SBC's actions, SBC could be required to pay WCG's transition costs of up to \$200 million, even though WCG's costs may be higher.

In June 2000, the FCC authorized SBC to provide long distance service in Texas. Under the terms of the strategic alliance with SBC, WCG is the preferred provider of SBC's nationwide long distance voice and data services. WCG began providing services in Texas in July 2000. More recently, the FCC authorized SBC to provide long distance services in Kansas and Oklahoma beginning on March 7, 2001, although certain would-be competitors are challenging this order in the federal courts.

In June 2000, WCG acquired SBC's initial party interests in two undersea communications cables between the United States and China and Japan, respectively. In September 2000, WCG acquired the long distance network assets of Ameritech Communications, Inc., a subsidiary of SBC.

The assets are located in the states of Illinois, Indiana, Michigan, Ohio, and Wisconsin, and include a fiber-optic network, data centers, indefeasible rights of use in dark fiber, and switches. In connection with this purchase of the Ameritech assets, the services agreement with SBC was amended to require Ameritech to buy services from WCG.

WCG has entered into a services agreement with SBC by which WCG will provide local transport services to SBC in six markets: New York, Boston, Seattle, Phoenix, Atlanta, and Denver. This agreement provides for expansion of the services in these markets and further expansion into additional markets.

Intel Corporation. Intel is a manufacturer of chips and other computer, networking, and communications products. The Intel® Internet Media Services business provides Internet web-hosting services by building and managing data centers around the world that will support the web sites of third parties. At the time of the WCG initial public offering, Intel acquired 9,225,093 shares of WCG's common stock, which represents approximately two percent of the shares of capital stock outstanding as of February 28, 2001.

On May 24, 1999, WCG entered into a 10-year master alliance agreement with Intel. WCG and Intel Internet Media Services will purchase services from one another pursuant to a services agreement entered into on July 13, 1999. On the same date WCG also entered into a sales representative agreement. Both agreements are for a three-year term renewable for one-year terms thereafter. WCG is currently providing domestic transport services to Intel and anticipates that Intel will provide web-hosting services to WCG. Subject to meeting price, quality of service, and other specifications, Intel Internet Media Services will purchase a significant portion of its yearly domestic transport requirements from WCG. In addition, in May 2000, Intel Internet Media Services agreed to use the WCG network to deliver high-performance streaming media to its Internet users. In connection with its purchase of the WCG common stock, Intel has agreed not to transfer any of its shares of WCG common stock to anyone except affiliates until April 2001, but this restriction will terminate if WCG has a change of control. The transfer restriction does not prohibit Intel from selling shares in future registered offerings initiated by WCG or from engaging in hedging transactions. Intel also has the right to require WCG to register under the Securities Act its shares of WCG Class A common stock.

Teléfonos de México, S.A. de C.V. Teléfonos de México, S.A. de C.V., the largest communications provider in Mexico, currently provides long distance and local services primarily in Mexico. At the time of the WCG initial public offering, on October 6, 1999, Teléfonos de México acquired 4,612,546 shares of WCG Class A common stock, which represents approximately one percent of the shares of capital stock outstanding as of February 28, 2001. In connection with its purchase of WCG common stock, Teléfonos de México has agreed to certain restrictions and will receive certain privileges, including the following:

- Teléfonos de México has a right to be notified and given an opportunity to acquire additional shares of WCG common stock which cannot exceed a total ownership interest of 10 percent of all classes of WCG common stock outstanding on a combined basis until at least 2009.
- Teléfonos de México has agreed not to transfer to anyone, except affiliates, any of its shares of WCG common stock until April 2003, unless WCG had a change of control.
- Teléfonos de México has agreed that WCG has the right, until April 2003, to repurchase WCG stock at market value less the underwriter's discount if the alliance agreement is terminated for any reason other than a breach by WCG.
- Teléfonos de México also has the right to require WCG to register under the Securities Act its shares of WCG common stock.

In addition, Williams, so long as it has a 50 percent equity interest in WCG, has a right of first purchase with respect to any shares of WCG common stock that Teléfonos de México should decide to offer. WCG also has a right of first purchase with respect to any shares of common stock not purchased by Williams.

On May 25, 1999, WCG entered into an alliance agreement with Teléfonos de México under which, subject to any necessary U.S. and Mexican regulatory requirements:

- Until 2019, Teléfonos de México must first seek to obtain select international wholesale services and various other services from WCG.
- Until 2019, WCG must first seek to obtain select international wholesale services and various other services from Teléfonos de México.
- WCG and Teléfonos de México will sell each other's products to their respective customers and will negotiate the terms under which both parties will provide installation and maintenance of communications equipment and other services for the other.

For the services each must seek to obtain from the other, the prices generally will be established to reflect the strategic relationship and commitments made to each other, subject to any applicable law or regulations establishing the prices. If either party can secure lower prices for comparable services that the other party will not match, then that party is free to utilize the lowest cost provider. Both WCG and Teléfonos de México can provide services or products to other persons. Each party may also sell or utilize the products or services purchased from the other to provide products or services to other persons.

Certain of the provisions relating to the preferred provider relationship and competitive pricing requirements will not be implemented until changes to the international settlement system currently in place pursuant to U.S. and Mexican regulations occur. Due to Teléfonos de México's dominant position in Mexico, the international settlement system requires that Teléfonos de México split its switched traffic terminating in the United States on a basis proportionate to that of U.S. carriers terminating switched traffic in Mexico.

WCG and Teléfonos de México have agreed on a mechanism for the development of mutually beneficial projects intended to interconnect the WCG network with the Teléfonos de México network to provide seamless voice and data on both a nationwide and international basis. Project decisions will be based on the unanimous decision of committees composed of an equal number of representatives from WCG and Teléfonos de México.

Either party may terminate the alliance agreement if any of the following occurs:

- the action, or failure to act, of any regulatory authority or the passage of a law or regulation materially frustrates or hinders the purpose of any of the agreements
- either party experiences a change of control

One party may terminate the agreements if the other party materially breaches them or is no longer able to deliver the products and services for a period of 30 days.

In addition, WCG has entered into an interconnection agreement with Teléfonos de México and is negotiating additional agreements for the purchase and sale of telecommunications services. Under the proposed agreements, subsidiaries of Teléfonos de México will purchase internet transit services and voice services from WCG. WCG also intends to negotiate broader services and marketing agreements.

KDDI America. KDDI America, Inc. is a wholly owned subsidiary of DDI Corporation, the largest international telecommunications company in Japan. In June 2000, WCG entered into a comprehensive services agreement under which it will interconnect its network with KDDI America. In addition, KDDI America will first seek to obtain U.S. offered telecommunications services from WCG, and WCG will first seek to obtain Japan-terminating telecommunications services from KDDI America or DDI Corporation. WCG also agreed to collaborate with KDDI America on a number of other matters, including colocation services, e-business applications, and customer solutions.

Winstar. Winstar Communications, Inc. uses wireless technology to provide high-capacity local exchange and Internet access services to companies located generally in buildings not served by fiber-optic cable. WCG has entered into agreements with Winstar under which:

- Until 2023, WCG has a right to use approximately two percent of Winstar's wireless local capacity, which is planned to cover the top 50 U.S. markets, in exchange for payments equal to \$400 million over a period of four years.
- Until 2023, Winstar has a right to use four strands of WCG's fiber-optic cable over 15,000 route miles on the WCG network.
- Winstar has an obligation to lease specified circuits from WCG for at least 20-year terms.
- WCG has agreed to provide Winstar with colocation and maintenance services.
- Winstar will pay WCG \$644 million in equal monthly installments over a period of seven years ending in 2006, for providing the services noted above.

SOLUTIONS

On January 29, 2001, WCG announced a contract with Platinum Equity to sell the operations of its Solutions business segment in the United States and Mexico. In addition, it announced its intent to sell the remaining Canadian operations of Solutions in 2001. Under the terms of the Sale and Purchase Agreement by and among Williams Communications, LLC and certain of its subsidiaries and Platinum Equity, LLC, dated as of January 29, 2001, Platinum Equity will acquire Solutions' operations in the United States and Mexico as well as the Canadian professional services operations of Solutions.

Solutions installs, and maintains communications equipment and network services that provide solutions for the comprehensive voice and data needs of organizations of all sizes.

Products and Services

Solutions operates approximately 110 sales and service offices in the U.S., Canada, and Mexico staffed with approximately 1,000 sales personnel. Approximately 100 of Solutions' sales personnel focus on large national and government accounts. Solutions provides a comprehensive array of communications products and services, including equipment sales and service, professional services, and marketing of carrier services.

Vendor relationships

Solutions has agreements with the suppliers of the products and providers of the services it sells to its customers. These agreements provide for Solutions to distribute, resale, or integrate products or act as agent for the provider of services. Normally, Solutions receives volume discounts off the list price of the product or service it purchases from its vendors. Solutions' primary vendor relationships are with Nortel, Cisco, Lucent, and NEC, of which Nortel is the largest.

Customers

Solutions provides products and services to approximately 100,000 customer sites across a broad range of industries including businesses as well as educational, governmental, and non-profit institutions. These customers consist of small businesses (ten or more employees), small sites of larger companies, and large enterprise campus sites. Solutions is not dependent on any one customer or group of customers to achieve its desired results. Solutions' top 25 customers combined accounted for less than 25 percent of revenue during 2000, with no one customer accounting for more than 1 percent.

Competition

Solutions' competition comes from communications equipment distributors, network integrators, and manufacturers of equipment (including in some instances those manufacturers whose products Solutions also sells). Solutions' competitors include Norstan, Inc., Lucent, Siemens, Cisco Systems, and the equipment divisions of GTE, Sprint, and the regional Bell operating companies. Solutions operates in a highly competitive industry and faces competition from companies that may have significantly greater financial, technical, and marketing resources.

OTHER INFORMATION

Employees

As of December 31, 2000, WCG had a total of approximately 10,642 employees, 1,000 of whom were covered by collective bargaining agreements. The following shows the number of employees broken down by segment:

Network	2,611
Broadband Media	458
Strategic Investments	13
Corporate	1,308
Solutions	<u>6,252</u>
Total	<u>10,642</u>

Regulation

General Regulatory Environment

WCG is subject to federal, state, local, and foreign regulations that affect its product offerings, competition, demand, costs, and other aspects of its operations. U.S. federal laws and regulations generally apply to interstate telecommunications, including international telecommunications that originate or terminate in the United States, while state laws and regulations apply to telecommunications terminating within the state of origination. A foreign country's laws and regulations apply to telecommunications that originate or terminate in that country. The regulation of the telecommunications industry is changing rapidly and varies from state to state and from country to country. WCG's operations are also subject to a variety of environmental, safety, health, and other governmental regulations. WCG cannot guarantee that future regulatory, judicial, or legislative activities will not have a material adverse effect on it, or that domestic or international regulators or third parties will not raise material issues with regard to its compliance or noncompliance with applicable regulations.

The Telecommunications Act seeks to promote competition in local and long distance telecommunications services, including by allowing entities affiliated with power utilities entry into

providing telecommunications services and by allowing, subject to specified limitations and conditions, the regional Bell operating companies to enter the long distance market. WCG believes that the regional Bell operating companies' and other companies' entry into this market will provide opportunities for it to sell dark fiber or lease high-volume long distance capacity.

The Telecommunications Act allows a regional Bell operating company to provide long distance services originating outside its traditional exchange service area or from mobile services, and to own 10 percent or less of the equity of a long distance carrier operating in its traditional service area. In addition, Section 271 of the Telecommunications Act allows a regional Bell operating company to provide long distance services originating in a state in its traditional exchange service area if it satisfies several procedural and substantive requirements. These include obtaining FCC approval upon a showing that the regional Bell operating company has entered into, or under some circumstances has offered to enter into, interconnection agreements which satisfy a 14-point "checklist" of competitive requirements. On December 29, 1999, the FCC granted Bell Atlantic's petition to provide long distance service in New York State and, by order dated, June 30, 2000, authorized SBC to offer long distance services in Texas. More recently, the FCC granted SBC's petition to provide long distance service in Kansas and Oklahoma, and that authorization became effective on March 7, 2001. WCG expects that additional petitions for entry will be filed and that the regional Bell operating companies will obtain approval to provide long distance services in several other states within the next two years.

With certain exceptions, revenues derived from the provision of interstate and international telecommunications services to domestic end-users, including enhanced services providers, are subject to assessment for the FCC's Universal Service Fund, which assists in ensuring the universal availability of basic telecommunications services at affordable prices and other goals. The FCC announced assessments for first quarter of 2001 of approximately 6.7 percent of gross revenues subject to contribution. Some of WCG's services are subject to these assessments, which could increase its costs, and it may also be liable for assessments by state commissions for state universal service programs.

Federal Regulation

Under the FCC's rules, WCG is a non-dominant carrier. Generally, the FCC has chosen not to closely regulate the charges or practices of non-dominant carriers. Although the FCC has the power to impose more stringent regulatory requirements on non-dominant carriers, WCG believes that the FCC is unlikely to do so. WCG is subject to the regulatory requirements applicable to all common carriers, such as providing services without unreasonable discrimination and charging reasonable rates.

Federal regulation affects the cost and thus the demand for long distance services through regulation of interstate access charges, which are the local telephone companies' charges for use of their exchange facilities in originating or terminating interstate transmissions. The FCC, on May 31, 2000, ordered a multi-year transition in the structure of interstate access charges, leading to lower per-minute charges. Among some of the changes in that order, the FCC increased non-usage sensitive charges on local lines, eliminated non-usage sensitive charges on interexchange carriers, modified the productivity factor used in part to determine price caps on access charges for some local telephone companies, and created an explicit universal service component to recover some implicit subsidies in access charges that were effectively eliminated by the order. Some aspects of the FCC's access charge rules are subject to periodic review, and the agency may adopt further changes in the structure and levels of interstate access charges and other aspects intercarrier compensation in the future.

The FCC has adopted interconnection rules, including rules relating to pricing, for the provision of unbundled network elements and wholesale services by incumbent local telephone companies to competitive local telephone companies. The agency also adopted rules governing the physical colocation of competitive local telephone company equipment in certain of the incumbent local telephone companies' buildings to access unbundled network elements. Pursuant to interconnection agreements entered into with incumbent local telephone companies, competitive carriers may use these network elements, services, and colocation space to offer local services. Various aspects of these rules are subject to appeal and the FCC may alter portions of the rules in the future. These regulations affect growth opportunities for WCG and some of its customers that provide demand for its services.

The FCC has to date treated Internet service providers as enhanced service providers rather than common carriers. As such, Internet service providers have been generally exempt from various federal and state regulations, including the obligation to pay access charges and contribute to universal service funds.

The FCC has adopted rules for a multi-year transition to lower international settlement payments by U.S. common carriers, leading to lower rates for some international services and increased demand for these services provided by some of WCG's customers. The result is likely to be increased demand for capacity on the U.S. facilities, including its network, which provide these services.

The FCC commenced a transition period during which carriers must cancel most tariffs for interstate long distance services and cease filing new tariffs covering those services. By January 31, 2001, carriers were required to cancel customer specific tariffs. The FCC has set a deadline of July 31, 2001, for carriers to cancel tariffs covering most mass market interstate long distance services. The FCC further required those carriers with corporate websites to post information relating to the rates, terms, and conditions of such services on their websites. These actions may significantly affect the ability of Williams and its customers to rely on filed rates, terms, and conditions for interstate long distance services, the way these services are offered to customers, and the demand for such services. The FCC is considering the extension of a similar detariffing process to international services.

State Regulation

The Telecommunications Act generally prohibits state and local governments from enforcing any law, rule, or legal requirement that prohibits or has the effect of prohibiting any person from providing any interstate or intrastate telecommunications service. However, states retain jurisdiction to adopt regulations necessary to preserve universal service, protect public safety and welfare, ensure the continued quality of communications services, and safeguard the rights of consumers.

Generally, WCG must obtain and maintain certificates of authority from regulatory bodies in states in which it offers intrastate services. In most states, it must also file and obtain prior regulatory approval of tariffs for its regulated intrastate services. Certificates of authority can generally be conditioned, modified, or revoked by state regulatory authorities for failure to comply with state law or regulations. Fines and other penalties also may be imposed for such violations. WCG is currently authorized to provide intrastate services, at least to some extent, in 50 states and the District of Columbia. WCG believes that most states do not regulate its provision of dark fiber. If a state did regulate its provision of dark fiber, WCG could be required to provide dark fiber in that state pursuant to tariffs and at regulated rates.

State regulatory commissions generally regulate the rates incumbent local telephone companies charge for intrastate services, including intrastate access services paid by providers of intrastate long

distance services. WCG's local and other intrastate services compete against the regulated rates of these carriers and also use some of these services in providing its services. Under the Telecommunications Act, state commissions have jurisdiction to arbitrate and review negotiations between local telephone companies and competitive local exchange carriers regarding the prices local telephone companies charge for interconnection of network elements with, and resale of, services by competitive local exchange carriers; however, the Supreme Court has generally upheld the FCC's authority to adopt rules that the states must apply when setting these prices. WCG is entering into interconnection agreements with various incumbent local telephone companies and is considering others. These regulations, therefore, also affect its plans to offer such services. A state may also impose telecommunications taxes, and fees related to the support for universal service, on providers of services in that state.

Local Regulation

WCG is occasionally required to obtain street use and construction permits and licenses and/or franchises to install and expand its fiber-optic network using municipal rights of way. Termination or failure to renew its existing franchise or license agreements could have a material adverse effect on it. In some municipalities where it has installed or anticipates constructing networks, it is required to pay license or franchise fees based on a percentage of gross revenue or on a per linear foot basis. WCG cannot guarantee that fees will remain at their current levels following the expiration of existing franchises. In addition, WCG could be at a competitive disadvantage if its competitors do not pay the same level of fees as it does. However, the Telecommunications Act requires municipalities to manage public rights of way in a competitively neutral and non-discriminatory manner.

Other

WCG's operations are subject to a variety of federal, state, local, and foreign environmental, safety, and health laws, and governmental regulations. These laws and regulations govern matters such as the generation, storage, handling, use, and transportation of hazardous materials, the emission and discharge of hazardous materials into the atmosphere, the emission of electromagnetic radiation, the protection of wetlands, historic sites, and endangered species, and the health and safety of employees. Although a pending rulemaking commenced by the California Public Utilities Commission seeks to clarify and refine the agency's administration of environmental review for communications projects, Williams continues to face uncertainty on the extent of state regulatory authorizations and environmental review required to construct communications facilities in that state.

Although WCG monitors compliance with environmental, safety, and health laws and regulations, it cannot give assurances that it has been or will be in complete compliance with these laws and regulations. It may be subject to fines or other sanctions imposed by governmental authorities if it fails to obtain certain permits or violate the laws and regulations. No capital or other expenditures for compliance with laws, regulations, or permits relating to the environment, safety, and health were material in 2000.

In addition, WCG may be subject to environmental laws requiring the investigation and cleanup of contamination at sites it owns or operates or at third-party waste disposal sites. These laws often impose liability even if the owner or operator did not know of, or was not responsible for, the contamination. Although it owns or operates numerous sites in connection with its operations, it is not aware of any liability relating to contamination at these sites or third-party waste disposal sites that could have a material adverse effect on the company.

Foreign Regulation

The provision of telecommunications services in the countries in which WCG operates and intends to operate is regulated. Telecommunications carriers are generally required to obtain permits, licenses, or authorizations to initiate or terminate communications in a country. The regulatory requirements vary from country to country, although in some significant respects regulation in the Western European markets is harmonized under the regulatory structure of the European Union. Many regulatory systems have only recently faced the issues raised by competition and are still in the process of development. Telecommunications laws and regulations are changing generally to promote competition and new offerings. However, future regulatory, judicial, or legislative activities may have a material adverse effect on WCG, and international regulators or third parties may raise material issues with regard to its compliance or noncompliance with applicable regulations.

Generally, WCG must obtain and maintain authorizations from regulatory bodies in the countries in which it will offer telecommunications services. It may need different authorizations or no authorizations, depending on whether it constructs or leases its facilities, and whether it offers dark fiber, switched voice, private line, data, video, or enhanced services in many of the countries in which it plans to operate. WCG must also comply with environmental, planning, and property laws in those countries where it constructs and/or operates fiber-optic systems. In many countries, it must also file and obtain prior regulatory approval of the rates, terms, and conditions for its services. Authorizations can generally be conditioned, modified, or revoked by regulators for failure to comply with applicable laws or regulations. Fines and other penalties also may be imposed for violations. WCG expects to apply for and acquire various authorizations to operate its foreign facilities and provide its telecommunications services though it cannot guarantee that its licenses will not be delayed or include burdensome conditions.

Authorizations to operate as a new carrier are not available in some countries, may be available in other countries with limitations on the number and characteristics of carriers, and may not be required at all in other countries. In addition, while some countries require complex applications procedures for authorizations, some countries simply require registration with or notification to the regulatory agency. Within a country, moreover, some services or activities may require a full authorization while others may require a simple registration or notification, or no filing at all. Authorizations and regulations impose a range of restrictions on the carriers' operations, corporate governance, and shareholders, with penalties for noncompliance, including loss of license and monetary fines. For example, many countries place limits on foreign ownership of telecommunications carriers and require regulatory approval of transfers of control.

In granting authorizations, regulators frequently establish service obligations for the operator. Typical obligations include nondiscrimination, build-out or service coverage, and interconnection obligations, as well as requirements regarding the quality of service provided and the approval of new service offerings. Many regulators also require licensed carriers to pay certain fees or charges, including to cover the costs of regulation and to support the availability of services, and these fees may in some cases be significant.

Many national regulators require interconnection between carriers and resolve disputes as to the reasonableness of particular interconnection arrangements and pricing. Many regulators require a dominant carrier in the market to offer competing carriers interconnection on reasonable and nondiscriminatory terms and conditions, and a number of regulators are also beginning to require incumbent carriers to unbundle their local loops, allowing increasing competition in local services. In some countries, all telecommunications carriers are required to provide interconnection to other carriers. WCG may be required to provide interconnection to its foreign network as well as access to its facilities for the installation of other carriers' telecommunications equipment.

WCG may also be required to obtain street use and construction permits and licenses and/or franchises to install and expand its fiber-optic network using public rights of way. In some countries where it has installed or anticipates constructing networks, it may be required to pay license or franchise fees.

Submarine telecommunications cable systems require national authorizations from each country in which they land and operate. Cable landing authorizations typically involve environmental reviews as well as approvals by telecommunications authorities to provide international telecommunications facilities and services. In addition, municipal and state permits may be necessary. Any such authorization may be difficult to obtain or involve burdensome conditions. Telecommunications carriers using capacity on the cables usually need licenses from each country in which they operate and may need different licenses to provide different services. For example, WCG will need, and has applied for, a Public Telecommunications Operator license in the United Kingdom before providing services over the TAT-14 undersea cable.

Japan

WCG's Japanese subsidiary, Williams Communications K.K., has obtained a Type I license to land its interest in an undersea cable and to provide telecommunications services in Japan over this undersea cable. Before providing telecommunications services in Japan pursuant to its Type I license, WCG must meet a number of regulatory requirements.

Brazil

A cellular concession was granted to ATL in 1998 for an initial term of 15 years, which may be renewed for equal periods at the discretion of the national regulatory agency, Anatel. Currently, within each area, only two cellular companies may operate. In 2000, the government announced plans to sell additional licenses in each wireless market for personal communications service. The cellular concessions and other regulations impose a range of restrictions on the companies' operations, rates, services, corporate governance, and shareholders, with penalties for noncompliance, including loss of license and monetary fines.

United Kingdom

WCG's subsidiary in the United Kingdom, Williams Communications UK Limited, has received a Public Telecommunications Operator license to provide telecommunications services in the United Kingdom. This subsidiary intends to apply to the Office of Telecommunications for "Annex II" interconnection status, which will give it the right to interconnection with other carriers in the United Kingdom. The Public Telecommunications Operator license requires WCG's subsidiary to comply with a number of conditions, including but not limited to interconnection with other telecommunications companies and payment of license fees.

Australia

PowerTel holds a carrier license and is subject to regulation by the Australian Competition and Consumer Commission and the Australian Communications Authority. PowerTel does not have any service coverage obligations. PowerTel does not require any further regulatory approval for new services provided on its fiber-optic network.

Under the regulations, access to particular regulated carriage services and other services that facilitate the supply of those regulated services must be provided between operators on non-discriminatory technical and operational terms and, in some circumstances, at cost-based prices. Any transmission capacity of two or more megabits per second is regulated on all routes except between Sydney, Canberra, and Melbourne.

The Australian Competition and Consumer Commission has decided to regulate local call resale and local network unbundling. Regulation of interconnection at the local exchange level potentially allows PowerTel and other competitors to reduce their access costs by interconnecting with the Telstra Corporation Limited network closer to the customer.

PowerTel currently has entered into a facilities access agreement with Telstra for access to Telstra's ducts, underground facilities, and equipment buildings. PowerTel also obtains services from Telstra through wholesale/resale products and negotiating an agreement covering Telstra's wireline and mobile originating and terminating access services.

Chile

Chile currently has a competitive, multi-carrier system for long distance and local services. There is no regulatory limit on the number of concessions that could be granted to companies that would compete against Manquehue Net S.A. The largest providers of local telecommunications services in Santiago are Compania de Telecomunicaciones de Chile and CMET.

Manquehue Net holds an intermediate service concession for the installation, operation, and exploitation of a high-capacity fiber-optic cable network in Santiago and the towns surrounding it. Intermediate services are provided via networks to satisfy the transmission or exchange service requirements of other telecommunications providers. The concession is for a renewable 30-year term. Manquehue Net's concession provides for network construction to end on December 23, 1998, and service to begin on January 23, 1999. The company requested an extension of these terms, which was granted by the telecommunications authority but is pending before the Republic Comptrollership's Office for formal amendment of the concession.

The regulatory authority has declared that the conditions prevailing in the local (including Santiago) markets for Manquehue Net require that maximum rates to be determined for that company by the regulatory authority. Manquehue Net is not subject to a maximum rate for intermediate services. The maximum rate structure is determined every five years. Local providers must also give long distance service providers equal access to their network connections.

Settlement Costs for International Traffic

International switched long distance traffic between two countries historically is exchanged under correspondent agreements between carriers, each owning network transmission facilities in their respective countries. Correspondent agreements generally provide for, among other things, the termination of switched traffic in, and return switched traffic to, the carriers' respective countries at a negotiated accounting rate. Settlement costs, typically one-half of the accounting rate, are reciprocal fees owed by one international carrier to another for transporting traffic on its facilities and terminating that traffic in the other country. The FCC and regulators in foreign countries may regulate agreements between U.S. and foreign carriers.

The FCC's international settlements policy governs the settlements between U.S. carriers and their foreign correspondents and prevents foreign carriers from discriminating among U.S. carriers in bilateral accounting rate negotiations. The policy requires:

- the equal division of accounting rates
- non-discriminatory treatment of U.S. carriers
- proportionate return of inbound traffic

Agreements governed under the policy must be filed publicly with and approved by the FCC. The policy applies only to U.S. carrier arrangements with certain foreign carriers with market power

in their respective countries. For example, U.S. carrier arrangements with Teléfonos de México continue to be subject to the policy, but U.S. carrier arrangements with a Teléfonos de México competitor in Mexico are not subject to the policy. The FCC also recently decided to exempt certain foreign routes from the policy, depending upon the ability of U.S. carriers to terminate traffic on those routes at rates substantially below benchmarks set by the agency. However, Mexico is not currently an exempted route. Other countries have policies similar to that of the FCC.

Resale of international private lines allows carriers to bypass the settlement rate system, and, therefore, bypass the need to negotiate accounting rates with foreign carriers with market power and obtain termination of international traffic in the United States and foreign countries at substantially reduced rates. The FCC's private line resale policy currently prohibits a carrier from reselling international private leased circuits to provide switched services to or from a country unless certain conditions are met.

Currently, Mexican carriers other than Teléfonos de México can engage in such resale under FCC rules, but the Mexican regulator has not permitted such resale. If Mexico approves such resale but the FCC continues to restrict Teléfonos de México from engaging in such resale, competitors of Teléfonos de México would be permitted to engage in low-cost termination of traffic between the United States and Mexico, but Teléfonos de México would be precluded from doing so.

Forward-Looking Information

Certain matters discussed in this report, excluding historical information, include forward-looking statements — statements that discuss WCG's expected future results based on current and pending business operations. WCG makes these forward-looking statements in reliance on the safe harbor protections provided under the Private Securities Litigation Reform Act of 1995.

Forward-looking statements can be identified by words such as "anticipates," "believes," "expects," "planned," "scheduled" or similar expressions. Although WCG believes these forward-looking statements are based on reasonable assumptions, statements made regarding future results are subject to a number of risks, assumptions, and uncertainties that could cause WCG's actual results to differ materially from those projected. In addition to risk factors set forth in WCG's filings with the Securities and Exchange Commission, the following important factors could cause actual results to differ materially from any results projected, forecasted, estimated, or budgeted:

- Changes in general economic conditions in the United States and changes in federal or state laws and regulations to which WCG is subject, including tax, environmental, and employment laws and regulations.
- Changes in foreign economies, currencies, laws and regulations, and political climates, especially in Australia and South America, where WCG has made direct investments, and in Europe and Asia where WCG plans to provide transmission services.
- The cost and effects of legal and administrative claims and proceedings against WCG or its subsidiaries.
- Conditions of the capital markets WCG utilizes to access capital to finance operations.
- Termination of the SBC strategic alliance or SBC Communications' inability to obtain regulatory approval to provide long-distance communications services within markets in which it currently provides local services.
- The successful completion of the sale of the Solutions business and collection of the proceeds from the sale and on the receivables retained.
- Loss of a high volume Network customer.

- Technological developments, high levels of competition, lack of customer diversification, and general uncertainties of government regulation in the communications industry.
- Significant competition on pricing and product offerings for Network.
- The fact that Williams owns a significant majority of WCG and the potential need at a future date to replace, at a potentially higher cost, administrative services currently provided by Williams.
- The possible spin-off of shares of WCG's common stock held by Williams and the potential for amendments to the agreements between WCG and Williams that were entered into at the time of WCG's initial public offering.
- The effect of changes in accounting policies.
- The ability in a cost-effective way to raise capital needed to sustain operating cash flow, make capital expenditures, and meet debt obligations.
- The ability to attract and retain qualified employees.
- The ability to develop financial, management, and operating controls to manage costs and rapid growth.
- The ability of each operating segment to implement successfully key systems, such as order entry systems and service delivery systems, within currently estimated time frames and budgets.
- The ability to develop the "Williams Communications" brand.
- The ability to expand and enhance the network in response to customer demands and industry changes.
- The ability of Network to timely turn up service requests and minimize service interruptions.
- The ability to obtain additional capacity for the Williams network from other providers.
- The ability to expand the Williams network as needed to remain competitive and to maintain the Williams network's leading-edge technology.
- The ability to manage WCG's growth.
- The ability, in a cost-effective way, to obtain and maintain necessary rights of way for the Williams network.
- The ability to successfully market capacity on the Williams network.
- The realization of revenues from products and services in the early stages of development or operation.
- The ability to deploy sophisticated technologies on a local-to-global basis.
- The ability to successfully integrate any newly acquired businesses.

Item 2. *Properties*

The WCG network and its component assets are the principal properties that WCG currently operates. See Item 1(c), Narrative Description of Business — Properties, for a description of these properties. WCG leases portions of the network and related equipment pursuant to its asset defeasance program, which supplied funds to construct a portion of the network and purchase equipment. The lease term is for five years with possible renewal for two additional one-year terms. WCG has the rights to purchase or exchange the leased property during the lease term as well as to

purchase the property at the end of the lease term. The price at which WCG may purchase the property approximates its original cost. In the event WCG does not purchase the property at the end of the initial lease term, it is obligated to pay 89.9 percent of the original purchase cost of the property, reduced by payments made throughout the lease term.

The installed fiber-optic cable that is of the WCG network is laid under various rights of way. WCG has agreements in place for substantially all of the rights of way needed to complete its network. Almost all of its rights of way extend through at least 2018.

WCG owns or leases sites in approximately 125 U.S. cities on which it locates or plans to locate transmission, routing and switching equipment. These sites range in size from 2,000 square feet to 50,000 square feet and total approximately 1,700,000 square feet. WCG also leases office space in various locations, including from Williams. WCG leases from Williams approximately 1,200,000 square feet of office space in Tulsa, Oklahoma. On February 26, 2001, Williams contributed to WCG in exchange for shares of Class A Common Stock the Williams Technology Center, which is currently under construction and expected to be complete in fourth quarter 2001. Upon completion, the Williams Technology Center will provide approximately 700,000 square feet of office space and accommodate up to 4,000 employees. Upon completion, WCG will be able to terminate the majority of its Tulsa leases with Williams. Solutions occupies approximately 192,000 square feet of office space in Houston, Texas, which it subleases from Williams.

Item 3. *Legal Proceedings*

WCG is subject to various types of litigation in connection with its business and operations. However, with the possible exception of the landowner lawsuits described below, WCG does not believe that any pending litigation is material to its business or operations.

WCG and Williams Communications, LLC, a wholly owned operating subsidiary of WCG, are named as defendants in putative nationwide class actions or putative statewide class actions on behalf of all landowners on whose property the WCG allegedly installed fiber-optic cable without the permission of the landowner. WCG believes that installation of the cable containing the single fiber network that crosses over or near the putative class members' land does not infringe on their property rights. WCG also does not believe that the plaintiffs have sufficient basis for certification of a nationwide or statewide class.

It is likely that WCG will be subject to other putative class action suits challenging its nationwide rights of way. WCG cannot quantify the impact of all such claims at this time. Thus, WCG cannot be certain that the plaintiffs' putative class actions, if successful, will not have a material adverse effect upon its future financial position, results of operations or cash flows.

On September 7, 2000, All-Phase Utility Corp. amended its complaint in a matter originally filed June 28, 1999, against Williams Communications, LLC in the United States District Court for Oregon, alleging actual damages of at least \$236.5 million from loss of profit from potential construction and lost revenue from leases of fiber-optic cable and conduits plus punitive damages. All-Phase alleges that a portion of Williams Communications, LLC's Eugene, Oregon to Bandon, Oregon route is based on confidential information developed by All-Phase and that WCG breached its non-disclosure agreement with All-Phase and violated the Oregon Trade Secrets Act by using it. All-Phase also alleges that WCG misrepresented its plans for the route and that, as a result, All-Phase lost the opportunity to build its own line along the same route. On January 22, 2001, the Court entered an Order granting Williams Communications, LLC's Motion for Summary Judgment and dismissing the action. All-Phase did not appeal the Court's Order.

On December 20, 2000, the Women's Cooperative Trust Union filed a derivative shareholder action in the United States District Court for the Western District of Oklahoma against Williams,

WCG, and certain directors and officers alleging that certain named defendants were involved in the purchase of shares of stock at a reduced price of two corporations with which WCG had contracted for the purchase of telecommunication equipment. The allegations include breach of fiduciary duty, waste of corporate assets and usurpation of corporate opportunities. Plaintiff seeks compensatory damages, rescission of all transactions between the named individual officers and directors and the two corporations, including disgorgement of any profits, punitive damages, and attorneys' fees and costs.

On January 18, 2001, the attorneys representing Williams and WCG in their corporate capacity, as well as the attorneys representing the individual directors of Williams and WCG, filed Motions to Dismiss based upon failure to make a demand on the Boards and failure to plead demand futility with particularity. Counsel for Williams and WCG has also filed a motion requesting a transfer of the venue from the Western District of Oklahoma to the Northern District of Oklahoma. Defendants' motions remain pending.

Summary

WCG is a party to various other claims, legal actions and complaints arising in the ordinary course of business. With the possible exception of the putative class action suits described above, in the opinion of management, the ultimate resolution of all claims, legal actions and complaints after consideration of amounts accrued, insurance coverage, or other indemnification arrangements will not have a materially adverse effect upon WCG's future financial position, results of operations or cash flows.

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

Not applicable.

PART II

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

Williams Communications' Class A common stock is listed on the New York Stock Exchange under the symbol "WCG." At the close of business on February 28, 2001, Williams Communications had approximately 707 holders of record of its Class A common stock. No common stock cash dividends were made in 2000 or 1999. In addition, management does not expect to pay cash dividends on common stock in the foreseeable future as its current debt agreements place limitations on the payment of cash dividends. It is management's intention to retain future earnings, if any, to finance the operation and development of the business. Future dividends, if any, will be determined by the board of directors and will depend on the success of operations, capital needs, financial conditions, contractual restrictions and other factors that the board of directors considers. The high and low sales price ranges (composite transactions) are listed for the four quarters of 2000 and fourth quarter 1999, the first quarter that Williams Communications' Class A Common Stock was traded.

	<u>High</u>	<u>Low</u>
2000		
First Quarter	\$61.81	\$26.75
Second Quarter	\$51.31	\$30.31
Third Quarter	\$33.69	\$18.06
Fourth Quarter	\$21.13	\$ 9.50
1999		
Fourth Quarter	\$35.44	\$23.25