QUAGGA CORP
Form S-4
May 26, 2011
Table of Contents

As filed with the Securities and Exchange Commission on May 26, 2011

Registration No. 333-

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM S-4

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

PAETEC Holding Corp.

(Exact name of Registrant as specified in its charter)

Delaware	**4813**	**20-5339741**
(State or other jurisdiction of incorporation or organization)	**(Primary Standard Industrial Classification Code Number)**	**(I.R.S. Employer Identification No.)**

(For Co-Registrants, see Table of Co-Registrants on the following page)

One PAETEC Plaza

600 Willowbrook Office Park

Fairport, New York 14450

(585) 340-2500

(Address, including zip code, and telephone number, including area code, of Registrant s principal executive offices)

Arunas A. Chesonis

Chairman, President and Chief Executive Officer

PAETEC Holding Corp.

One PAETEC Plaza

600 Willowbrook Office Park

Fairport, New York 14450

(585) 340-2500

(Name, address, including zip code, and telephone number, including area code, of agent for service)

Copies to:

Richard J. Parrino, Esq. **Kevin K. Greenslade, Esq.**	**Mary K. O Connell, Esq.**
	Executive Vice President and General Counsel
Hogan Lovells US LLP	**PAETEC Holding Corp.**
555 Thirteenth Street, N.W.	**600 Willowbrook Office Park**
Washington, D.C. 20004	**Fairport, New York 14450**
(202) 637-5600	**(585) 340-2500**

Approximate date of commencement of proposed sale of the securities to the public: As soon as practicable after this registration statement becomes effective.

If the securities being registered on this Form are being offered in connection with the formation of a holding company and there is compliance with General Instruction G, check the following box. ¨

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨		Accelerated filer þ
Non-accelerated filer ¨	(Do not check if a smaller reporting company)	Smaller reporting company ¨

If applicable, place a check mark in the box to designate the appropriate rule provision relied upon in conducting this transaction:

Exchange Act Rule 13e-4(i) (Cross-Border Issuer Tender Offer)	¨
Exchange Act Rule 14d-1(d) (Cross-Border Third-Party Tender Offer)	¨

Table of Contents

CALCULATION OF REGISTRATION FEE

Title of each class of securities to be registered	Amount to be registered	Proposed maximum offering price per unit(1)	Proposed maximum aggregate offering price(1)	Amount of registration fee
9 7/8 % Senior Notes due 2018(2)	$450,000,000	100%	$450,000,000	$52,245
Guarantees of 9 7/8% Senior Notes due 2018(3)	N/A	N/A	N/A	N/A

(1) Estimated pursuant to Rule 457(f) under the Securities Act of 1933, solely for purposes of calculating the registration fee.

(2) The 9 7/8% Senior Notes due 2018 will be the obligations of PAETEC Holding Corp.

(3) Represents the guarantees of the 9 7/8% Senior Notes due 2018, to be issued by the Co-Registrants. Pursuant to Rule 457(n) under the Securities Act of 1933, no additional registration fee is being paid in respect of the guarantees.

The Registrants hereby amend this registration statement on such date or dates as may be necessary to delay its effective date until the Registrants shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933, as amended, or until the registration statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

TABLE OF CO-REGISTRANTS

Exact Name of Co-Registrant as Specified in its Charter	State or Other Jurisdiction of Incorporation or Organization	I.R.S. Employer Identification No.
PAETEC Corp.	Delaware	16-1551094
PAETEC Integrated Solutions Group, Inc.	Delaware	16-1585842
PAETEC iTel, L.L.C.	North Carolina	47-0903254
PaeTec Software Corp.	New York	16-1384745
US LEC LLC	Delaware	56-2065535
US LEC of Alabama LLC	North Carolina	56-2104211
US LEC of Florida LLC	North Carolina	56-2046424
US LEC of Maryland LLC	North Carolina	56-2117626
US LEC of North Carolina LLC	North Carolina	56-2091767
US LEC of South Carolina LLC	Delaware	56-2056428

US LEC of Tennessee LLC	**Delaware**	**56-2065536**
PaeTec Communications, Inc.	**Delaware**	**16-1551095**
PaeTec Communications of Virginia, Inc.	**Virginia**	**16-6486048**
US LEC Communications LLC	**North Carolina**	**56-2162051**
US LEC of Georgia LLC	**Delaware**	**56-2065537**
US LEC of Pennsylvania LLC	**North Carolina**	**56-2117625**
US LEC of Virginia L.L.C.	**Delaware**	**56-2012173**
Allworx Corp.	**Delaware**	**26-0259247**
MPX, Inc.	**Delaware**	**16-1468411**
Technology Resource Solutions, Inc.	**New York**	**51-0443765**
McLeodUSA LLC	**Delaware**	**42-1407240**
McLeodUSA Information Services LLC	**Delaware**	**76-0529757**
McLeodUSA Telecommunications Services, L.L.C.	**Iowa**	**42-1407242**
McLeodUSA Purchasing, L.L.C.	**Iowa**	**42-1501014**
U.S. Energy Partners LLC	**New York**	**14-1856903**
PAETEC Realty LLC	**New York**	**27-1866972**
Quagga Corporation	**California**	**87-0721393**
Cavalier Telephone Corporation	**Delaware**	**54-1946546**
CavTel Holdings, LLC	**Delaware**	**20-4208673**
Cavalier Telephone, L.L.C.	**Virginia**	**54-1914822**
Cavalier Telephone Mid-Atlantic, L.L.C.	**Delaware**	**54-2028580**
SM Holdings, LLC	**Delaware**	**26-0970378**
Cavalier IP TV, LLC	**Delaware**	**20-2386185**
Elantic Networks, Inc.	**Delaware**	**20-0726068**
Intellifiber Networks, Inc.	**Virginia**	**54-1861675**
Cavalier Services, LLC	**Delaware**	**20-2047841**
Talk America Holdings, Inc.	**Delaware**	**23-2827736**
Talk America Inc.	**Pennsylvania**	**23-2582790**
TC Services Holding Co., Inc.	**Pennsylvania**	**23-3036795**
LDMI Telecommunications, Inc.	**Michigan**	**38-2940840**
NT Corporation	**Delaware**	**59-3619111**
Network Telephone Corporation	**Florida**	**59-3477521**
Compco, Inc.	**Delaware**	**23-2940793**
Talk America of Virginia, Inc.	**Virginia**	**54-1871946**
Access One Communications Corp.	**New Jersey**	**22-3527935**
OmniCall, Inc.	**South Carolina**	**57-1046947**
The Other Phone Company, Inc.	**Florida**	**65-0705374**

Address, including zip code, and telephone number, including area code, of each Co-Registrant s principal executive offices and each Co-Registrant s agent for service is c/o PAETEC Holding Corp., One PAETEC Plaza, 600 Willowbrook Office Park, Fairport, New York, 14450, and the name of each Co-Registrant s agent for service is Arunas A. Chesonis, Chairman, President and Chief Executive Officer, PAETEC Holding Corp.

The Primary Standard Industrial Classification Code Number for each Co-Registrant is 4813.

Table of Contents

The information in this prospectus is not complete and may be changed. We may not sell these securities until the registration statement filed with the Securities and Exchange Commission is effective. This prospectus is not an offer to sell these securities and is not soliciting an offer to buy these securities in any state where the offer or sale is not permitted.

Subject to completion, dated May 26, 2011

PROSPECTUS

PAETEC Holding Corp.

Offer To Exchange Up To

$450,000,000

9 7/8% Senior Notes due 2018

which have been registered under the Securities Act of 1933

for any and all outstanding

9 7/8% Senior Notes due 2018

The Exchange Offer:

The notes offered by this prospectus, or exchange notes, have been registered under the Securities Act of 1933, as amended, and are being offered in exchange for the outstanding, unregistered notes, or original notes, that were originally issued on December 2, 2010.

We will exchange all original notes that are validly tendered and not withdrawn prior to the expiration of the exchange offer for an equal principal amount of exchange notes.

The exchange offer will expire at 5:00 p.m., New York City time, on , 2011, unless extended by us.

You may withdraw tendered outstanding original notes at any time prior to the expiration of the exchange offer.

The exchange of outstanding original notes for exchange notes pursuant to the exchange offer generally will not be a taxable event for U.S. federal income tax purposes.

We will not receive any proceeds from the exchange offer.

The Exchange Notes:

The terms of the exchange notes will be substantially identical to the terms of the original notes, except that the exchange notes are registered under the Securities Act, and the transfer restrictions, registration rights and related additional interest terms applicable to the original notes will not apply to the exchange notes.

The exchange notes will mature on December 1, 2018. We will pay interest on the exchange notes semi-annually on June 1 and December 1 of each year.

The exchange notes will be guaranteed on a senior unsecured basis by each of our existing and future domestic restricted subsidiaries, other than certain excluded subsidiaries.

We do not intend to list the exchange notes on any securities exchange.

Any broker-dealer that holds original notes acquired for its own account as a result of market-making activities or other trading activities, and that receives exchange notes pursuant to the exchange offer, must deliver a prospectus in connection with any resales of such exchange notes. We have agreed that, for a period beginning on the date the exchange offer is consummated and ending on the earlier of 180 days after the date of this prospectus and the date on which a broker-dealer is no longer required to deliver a prospectus in connection with market-making activities or other trading activities, we will make this prospectus, as amended or supplemented, available to any broker-dealer for use in connection with any such resale. For more information, see Plan of Distribution.

Investments in the exchange notes involve risks. See Risk Factors beginning on page 11.

Neither the Securities and Exchange Commission nor any state securities commission nor any other regulatory body has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is , 2011.

TABLE OF CONTENTS

Table of Contents

SUMMARY

This summary highlights selected information included in this prospectus. This summary is not intended to be a complete description of the matters covered in this prospectus and is subject to, and qualified in its entirety by, reference to the more detailed information and financial statements (including the notes thereto) included in this prospectus.

Unless otherwise indicated or required by the context, references in this prospectus to we, us, our and PAETEC mean PAETEC Holding Corp. and its consolidated subsidiaries as of the date of such reference. References in this prospectus to PAETEC Holding mean PAETEC Holding Corp. and none of its subsidiaries.

Our Company

We are a competitive broadband communications services and solutions provider guided by the principle that delivering superior customer service is the key to competing successfully with other communications services providers. Our primary business is providing business end-user customers in metropolitan areas with a package of integrated broadband services that encompasses data services, including Internet access services and virtual private network services, and voice services, including local telephone services and domestic and international long distance services. As of March 31, 2011, we provided services for over 54,000 business customers in a service area encompassing 86 of the top 100 metropolitan statistical areas.

We focus our network services marketing efforts on medium-sized and large businesses and institutions. By focusing our marketing efforts on these larger businesses and institutions that have significant communications needs, we believe that we achieve a competitive advantage over larger carriers that target a broad cross-section of residential, business and institutional customers. Our focus on providing superior customer service begins with the sales process. Our management emphasizes the importance of attracting, training, motivating, and retaining skilled sales professionals. When meeting with a potential customer, members of our sales force rely on our internally-developed proprietary software to tailor services packages and pricing to meet the particular needs of each customer. Our sales force is supported by sales engineers and account development representatives who facilitate the initial provisioning of services and develop customer relationships that we seek to strengthen over time. We believe that our tailored pricing and service offerings and our dedicated account development programs are significant factors in customer retention.

We emphasize network technology as an element of our business strategy to the extent that this element supports our delivery of high-quality and reliable service. We have deployed a flexible and reliable open technology network that allows us to support newer technologies, including service offerings based on Internet Protocol, or IP. In addition, this network design allows us to offer our customers flexible technological solutions, reduce our total capital investments and apply increased capital to our sales and customer service support systems.

Our Strengths

We believe that the following strengths will help us to execute our strategy:

Our focus on medium-sized and large businesses and institutions that have significant communications needs, require complex integrated services and value superior customer support. We believe that our target customers most frequently make their communications purchase decisions based on a combination of factors in which the quality of customer service is as important as service offerings and price. By focusing on these customers, we believe that we are able to use our focus on customer service and our bundled service offerings to win new business, to minimize customer turnover and to sell an increasing number of products and services to each account as the customer relationship matures. We believe that recent consolidation in the industry has resulted in these customers being underserved by many of the larger carriers. Our customer base is characterized by low turnover and high monthly recurring revenue.

Our experienced direct sales force and effective distribution channels. We market our services through our direct sales force and through independent sales agents located throughout our markets. Our direct sales force and agents work closely with potential and existing customers to design tailored services bundles that meet unique and evolving customer needs. Our technology enables our sales force to identify and acquire targeted customers rapidly and to tailor and price a variety of service choices to match a customer s specific requirements. We seek to hire experienced sales professionals, and we supplement the experience of our employees and sales agents by providing them with intensive training in our service offerings and in marketing our services in selected industry sectors. We seek to motivate and retain our sales employees, sales agents and agent support personnel with commissions and, in some circumstances, long-term equity incentives. Our employee-oriented focus helps to foster a motivated sales force that we believe is essential to providing superior customer service.

Our broad-based, asset-rich, multi-platform network. We maintain one of the largest competitive networks nationwide, with approximately 36,700 route miles of fiber, including approximately 10,600 metro route miles, as of March 31, 2011. In addition, we manage a broad-based network with both traditional analog and next generation IP-switching intelligence at the core of our network, facilitating our provision as of March 31, 2011 of a wide range of sophisticated solutions offerings in 86 of the top 100 metropolitan statistical areas nationwide. This network enables us to provide flexible and customer-specific solutions while maintaining significant control over the quality and consistency of service. We believe that the flexibility and reliability of our existing network allows us to provide a superior customer experience at a reasonable price. As part of our network strategy, we connect our customers to our network primarily by leasing special access digital T1 transmission lines that we believe facilitate very fast installation times and decreased customer outages. We lease a significant portion of these special access lines through competitively priced bulk purchase agreements with other communications companies and internally manage the service quality on those lines through our multiple network operations centers.

Our proven management team. Our management team has an established track record of accomplishments in the communications industry. Several members of our senior management team and a significant number of additional individuals whom we have employed since we commenced operations in 1998 previously worked together for several years at ACC Corp., which was the first competitive carrier to use a similar network deployment strategy to ours of leasing, rather than building, telephone and data transmission lines. Our executive officers have an average of 19 years of experience in the telecommunications industry and are experienced in the integration of acquired businesses.

Our Strategy

Our objective is to be the most customer- and employee-oriented communications services provider to medium-sized and large businesses and institutions in our markets. To accomplish this objective, we seek to:

Provide superior service and customer care through a highly motivated and committed workforce. We believe that our target customer base, which is composed primarily of medium-sized and large businesses and institutions, is often underserved by traditional telephone companies. Based on our experience, we also believe that many communications providers continue to focus primarily on the technology associated with delivering access, transport and basic voice and Internet access services, rather than on the customer service and consultative sales relationships that attract and retain customers and support the delivery of those services. We seek to gain a competitive advantage and differentiate ourselves from other carriers by building long-term customer relationships based on providing consistent and superior customer service. We believe that our dedicated employee base, employee training programs, billing and back office systems, customer service response teams and reliable network connections provide us with this competitive advantage. We seek to provide incentives to our dedicated workforce, which totaled approximately 4,500 employees at March 31, 2011, through an attractive combination of cash compensation, equity ownership, other benefits, employee recognition awards and a flexible work environment. We believe that this blend of incentives attracts committed, motivated and loyal employees who strive to deliver high levels of service to promote customer satisfaction.

Offer a broad range of advanced and traditional communications services. We offer a flexible variety of network services, including our local and long distance voice services and our integrated data services, as an integrated package that is delivered over the same digital transmission lines. In addition, our flexible network enables us to provide advanced IP-based offerings, such as Voice over Internet Protocol, or VoIP, services and MultiProtocol Label Switching Virtual Private Network, or MPLS VPN, services. We attempt to augment our network services bundle with value-added integrated solutions, such as our proprietary telecommunications management software applications and our network integration offerings, that help to differentiate our services bundle from the services of our competitors and often to attract new customers. As a result, our customers frequently are able to fulfill their communications services requirements through one point of contact and receive a monthly statement of charges for a full range of communications services on one integrated bill.

Work closely with customers to develop end-to-end communications solutions tailored to their particular needs. We believe that our sales and service approach, in which we consult with our customers to design services customized to meet their particular needs, is an effective strategy for attracting and retaining customers with complex communications needs. We have established local sales offices and hired sales personnel in each of our markets to provide an experienced, local account management team that offers face-to-face sales and personalized client care for our entire service offering. We believe that our service-driven customer relationship strategy results in high levels of customer satisfaction and will lead to an increase in demand for our services. By serving the specific needs of customers in several industries, we believe we are well-equipped to attract new customers in those industries and to sell additional services to existing customers.

Use existing customer base and industry expertise to introduce new products and services and to expand selectively into new markets. We use relationships with our customers in existing markets to introduce new products and services. We believe that our close relationships with our customers and our dedication to customer service fosters an environment for the introduction of new products and services that we believe may benefit the customer. We also seek to penetrate markets further and expand our network services business into new markets through our integrated solutions offerings. We frequently use these offerings to establish new customer relationships. Once a customer has purchased one of our offerings, our goal is to become the provider of choice for all of that customer s communications needs by providing superior customer support. As we offer and sell our integrated solutions on a stand-alone basis to customers outside of our markets when we believe it is
economically or strategically advantageous, we seek to use these customers as reference accounts to increase penetration of existing geographic markets and industries with our network services and to expand into new geographic markets and industries.

Selectively supplement internal growth through targeted acquisitions. To supplement our internal growth, we have pursued an acquisition strategy focused on acquisition candidates that fulfill one or more key objectives. The objectives include increasing our penetration of current markets, expanding

Table of Contents

into new markets, augmenting the geographic scope of our network fiber-based assets (primarily in high density markets), and enhancing our ability to sell and deliver value-added services. We continue to seek acquisition candidates that will add customers and cash flow to our existing network services business or that will enhance our operating efficiencies by lowering access costs through the provision of fiber-based assets. In accordance with this strategy, we focus our acquisition efforts on other competitive carriers, on local and long distance providers, on enhanced service providers, on network integrators and on equipment solution providers. From time to time, we may consider selective acquisitions of those types of businesses that we believe will enhance our package of service offerings, increase our customer base and bring experienced back office, technical and customer service personnel to our company.

Our Corporate Information

PAETEC Holding Corp. was incorporated in Delaware in August 2006. PAETEC Holding Corp. is a holding company that conducts its operations through wholly-owned subsidiaries. The mailing address of PAETEC Holding Corp. s principal executive offices is One PAETEC Plaza, 600 Willowbrook Office Park, Fairport, New York 14450, and its telephone number is (585) 340-2500. We maintain a corporate Internet web site at www.paetec.com. Our website is not a part of this prospectus and is included as an inactive textual reference only.

Table of Contents

The Exchange Offer

In November 2010, PAETEC Holding formed PAETEC Escrow Corporation, or the Escrow Issuer, a Delaware corporation and wholly-owned subsidiary of PAETEC Holding, solely for the purpose of issuing the 9 7/8% Senior Notes due 2018, which we refer to as the original notes. On December 2, 2010, the Escrow Issuer completed the offering of $450,000,000 aggregate principal amount of original notes, and the gross proceeds of the offering, together with certain additional amounts, were deposited into a segregated escrow account. On December 6, 2010, upon the satisfaction of the escrow conditions, PAETEC Holding assumed the Escrow Issuer s obligations and agreements under the original notes, the indenture governing the original notes and the related registration rights agreement, and the proceeds of the offering of the original notes were disbursed from the escrow account and used, together with cash on hand, to pay the merger consideration and the other costs and expenses related to PAETEC Holding s acquisition of Cavalier Telephone Corporation, or Cavalier, on that date.

The offering of the original notes was made in transactions not requiring registration under the Securities Act of 1933, as amended, or Securities Act. In connection with our assumption of the original notes, we entered into a registration rights agreement with the initial purchasers of such notes in which we agreed, among other things, to deliver this prospectus and to complete an exchange offer for the original notes. Below is a summary of the exchange offer.

The Exchange Offer	We are offering to exchange $1,000 principal amount of our 9 7/8% Senior Notes due 2018, which have been registered under the Securities Act and which we refer to as the exchange notes, for each $1,000 principal amount of our outstanding, unregistered original notes. Unless we specify otherwise or the context indicates otherwise, we refer to the exchange notes and the original notes together as the notes.
	To be exchanged, an original note must be properly tendered and accepted. All original notes that are validly tendered and not withdrawn will be exchanged. As of the date of this prospectus, there are $450,000,000 aggregate principal amount of original notes outstanding. We will issue exchange notes promptly after the expiration of the exchange offer.
Resales of Exchange Notes	Based on interpretations by the staff of the Securities and Exchange Commission, or SEC, in no-action letters issued to third parties with respect to other transactions, we believe that the exchange notes issued in the exchange offer may be offered for resale, resold or otherwise transferred by you without compliance with the registration and prospectus delivery requirements of the Securities Act as long as:
	you are acquiring the exchange notes in the ordinary course of your business;
	you have no arrangement or understanding with any person to participate in a distribution of the exchange notes; and
	you are not our affiliate within the meaning of Rule 405 under the Securities Act, which defines affiliate as a person that, directly or indirectly, controls or is controlled by, or is under common control with, a specified person.

Table of Contents

	If you do not satisfy the foregoing conditions, in the absence of an exemption, you must comply with the registration and prospectus delivery requirements of the Securities Act in connection with the resale of the exchange notes. If you fail to comply with these requirements, you may incur liabilities under the Securities Act, and we will not indemnify you for such liabilities.
	Each broker-dealer that receives exchange notes for its own account in exchange for original notes that were acquired as a result of market-making activities or other trading activities must acknowledge that it will comply with the registration and prospectus delivery requirements of the Securities Act in connection with any offer to resell, resale or other transfer of the exchange notes issued in the exchange offer. We have agreed in a registration rights agreement that, for a period beginning on the date the exchange offer is consummated and ending on the earlier of 180 days after the date of this prospectus and the date on which a broker-dealer is no longer required to deliver a prospectus in connection with market-making activities or other trading activities, we will make this prospectus, as amended or supplemented, available to any broker-dealer for use in connection with any such resale. For additional information, see Plan of Distribution.
Expiration Date	The exchange offer will expire at 5:00 p.m., New York City time, on , 2011 unless extended by us.
Withdrawal Rights	You may withdraw tenders of the original notes at any time prior to the expiration of the exchange offer. For additional information, see The Exchange Offer Terms of the Exchange Offer.
Conditions to the Exchange Offer	The exchange offer is subject to customary conditions, which we may waive in our sole discretion, subject to applicable law. For additional information, see The Exchange Offer Conditions to the Exchange Offer. The exchange offer is not conditioned upon the exchange of any minimum principal amount of original notes.
Procedures for Tendering Original Notes	If you wish to accept the exchange offer, you must (1) complete, sign and date the accompanying letter of transmittal, or a facsimile copy of such letter, in accordance with its instructions and the instructions in this prospectus, and (2) mail or otherwise deliver the executed letter of transmittal, together with the original notes and any other required documents, to the exchange agent at the address set forth in the letter of transmittal. If you are a broker, dealer, commercial bank, trust company or other nominee and you hold original notes through The Depository Trust Company, or DTC, and wish to accept the exchange offer, you must do so pursuant to DTC s procedures. For additional information, see The Exchange Offer Procedures for Tendering.

Table of Contents

	If you are a beneficial owner whose original notes are registered in the name of a broker, dealer, commercial bank, trust company or other nominee and you wish to tender your original notes in the exchange offer, we urge you to contact promptly the person or entity in whose name your original notes are registered and instruct that person or entity to tender those notes on your behalf. If you wish to tender original notes in the exchange offer on your own behalf, you must, prior to completing and executing the letter of transmittal and delivering your original notes, either make appropriate arrangements to register ownership of your original notes in your name or obtain a properly completed bond power from the person or entity in whose name your original notes are registered. The transfer of registered ownership may take considerable time.
Guaranteed Delivery Procedures	If you wish to tender your original notes and your original notes are not immediately available or you cannot deliver your original notes, the letter of transmittal or any other required documents to the exchange agent (or comply with the procedures for book-entry transfer) prior to the expiration date, you must tender your original notes according to the guaranteed delivery procedures set forth in The Exchange Offer Guaranteed Delivery Procedures.
Consequences of Failure to Exchange	If you do not exchange your original notes, they will remain entitled to the rights and subject to the limitations contained in the indenture governing the notes. Following the exchange offer, however, all outstanding original notes will continue to be subject to the same restrictions on transfer, and we will have no obligation to register outstanding original notes under the Securities Act or to pay contingent increases in interest based on our original registration obligation.
Use of Proceeds	We will not receive any proceeds from the exchange offer.
Exchange Agent	The Bank of New York Mellon Trust Company, N.A. is serving as the exchange agent in connection with the exchange offer. The address, telephone number and facsimile number of the exchange agent are listed in The Exchange Offer Exchange Agent.

Table of Contents

The Exchange Notes

The exchange offer relates to the exchange of up to $450,000,000 aggregate principal amount of original notes for an equal principal amount of exchange notes. The terms of the exchange notes will be substantially identical to the terms of the original notes, except that the exchange notes are registered under the Securities Act and the transfer restrictions, registration rights and related additional interest terms applicable to the original notes will not apply to the exchange notes. The exchange notes will evidence the same indebtedness as the original notes which they will replace. The exchange notes will be governed by the same indenture as the original notes.

Issuer	PAETEC Holding Corp.
Notes Offered	$450,000,000 aggregate principal amount of 9 7/8% Senior Notes due 2018.
Maturity Date	December 1, 2018.
Interest Payment Dates	June 1 and December 1 of each year.
Guarantees	The exchange notes will be guaranteed on a senior unsecured basis by each of our existing and future domestic restricted subsidiaries, other than certain excluded subsidiaries.
Ranking	The exchange notes will be the general senior unsecured obligations of PAETEC Holding and will rank equally in right of payment with all of PAETEC Holding s existing and future senior indebtedness, including the indebtedness under its existing 9.5% Senior Notes due 2015, which we refer to as the 9.5% senior notes. As of the date of this prospectus, PAETEC Holding had outstanding $300 million aggregate principal amount of 9.5% senior notes. The exchange notes will rank senior in right of payment to all of PAETEC Holding s existing and future subordinated indebtedness. The exchange notes will be effectively subordinated in right of payment to all of PAETEC Holding s existing and future secured obligations, to the extent of the value of the collateral securing such obligations. As of March 31, 2011, PAETEC Holding s secured obligations included its senior secured credit facilities and its existing 8 7/8% Senior Secured Notes due 2017, which we refer to as the 8 7/8% senior secured notes, of which an aggregate principal amount of $650 million was outstanding. We sometimes refer to the 9.5% senior notes and the 8 7/8% senior secured notes together as the existing notes. The exchange notes will be structurally subordinated to any existing and future indebtedness and liabilities of our subsidiaries that are not subsidiary guarantors. The guarantee of the exchange notes by each subsidiary guarantor will be the general senior unsecured obligation of that subsidiary guarantor and will rank equally in right of payment with all of such subsidiary guarantor s existing and future senior indebtedness, including the guarantees of the 9.5% senior notes. The guarantee of each subsidiary guarantor will rank senior in right of payment to all of

Table of Contents

	such subsidiary guarantor s existing and future subordinated indebtedness, and will be effectively subordinated in right of payment to all of such subsidiary guarantor s existing and future secured obligations, including its guarantees of PAETEC Holding s existing senior secured credit facilities and the 8 $^{7}/8$% senior secured notes, to the extent of the value of the collateral securing such obligations.
	As of March 31, 2011, following the closing of the offering of the original notes and our use of the net offering proceeds to pay the merger consideration and other costs and expenses related to our acquisition of Cavalier, we had $1,425 million aggregate principal amount of senior indebtedness outstanding, $675 million of which was senior secured indebtedness.
Optional Redemption	We may redeem some or all of the exchange notes, at any time before December 1, 2014, at a redemption price equal to 100% of their principal amount plus a make-whole premium, together with accrued and unpaid interest, if any, to, but excluding the redemption date. We may redeem some or all of the exchange notes, at any time on or after December 1, 2014, at the redemption prices described in this prospectus, together with accrued and unpaid interest, if any, to, but excluding, the redemption date.
	Before December 1, 2013, we may redeem up to 35% of the aggregate principal amount of the notes and any additional notes initially issued under the indenture that will govern the exchange notes at a redemption price equal to 109.875% of the principal amount thereof, plus accrued and unpaid interest, if any, to, but excluding, the redemption date, with the net cash proceeds of one or more equity offerings, except that at least 65% of the principal amount of the notes and any such additional notes initially issued must remain outstanding immediately after giving effect to such redemption. For additional information, see Description of the Exchange Notes Optional Redemption.
Mandatory Offers to Purchase	If we experience certain kinds of changes of control, we must offer to repurchase the exchange notes at 101% of their principal amount, plus accrued and unpaid interest. For additional information, see Description of the Exchange Notes Certain Covenants Repurchase of Notes Upon a Change of Control.
	If we sell certain of our assets and do not apply the net proceeds to repay indebtedness under our senior secured credit facilities, the 8 $^{7}/8$% senior secured notes or other indebtedness secured on a first-priority basis or to reinvest in our business, we must offer to purchase the exchange notes at 100% of their principal amount, plus accrued and unpaid interest. For additional information, see Description of the Exchange Notes Certain Covenants Limitation on Asset Sales.

Certain Covenants	The indenture that will govern the exchange notes contains covenants that, among other things, limit our ability and the ability of our restricted subsidiaries to:
	incur or guarantee additional indebtedness;
	pay dividends on, redeem or repurchase our capital stock;
	make investments or repay subordinated indebtedness;
	engage in sale-leaseback transactions;
	enter into transactions with affiliates;
	sell assets;
	create liens;
	create restrictions on dividend and other payments to us from our subsidiaries;
	issue or sell stock of subsidiaries; and
	engage in a merger or consolidation, or sell, transfer or otherwise dispose of all or substantially all of our assets.
	All of the covenants are subject to a number of important qualifications and exceptions that are described under Description of the Exchange Notes.
Taxation	The exchange pursuant to the exchange offer generally will not be a taxable event for U.S. federal income tax purposes.
	Because the original notes were issued with original issue discount, or OID, for U.S. federal income tax purposes, the exchange notes will be treated as having been issued with OID. U.S. holders generally will be required to include such OID in their income as it accrues for U.S. federal income tax purposes in advance of the receipt of any payment on the exchange notes to which the income is attributable. For additional information, see U.S. Federal Income Tax Considerations Consequences to U.S. Holders.

10

Table of Contents

RISK FACTORS

Before you participate in the exchange offer, you should carefully consider the various risks of the investment, including the risks described below, together with all of the other information included in this prospectus. If any of these risks actually occurs, our business, financial condition or operating results could be adversely affected. These risks also could materially affect our ability to meet our obligations under the exchange notes. You could lose all or part of your investment in, and the expected return on, the exchange notes.

Risks Related to Investing in the Exchange Notes

Our significant level of debt and interest payment obligations may limit our ability to compete and prevent us from meeting our obligations under the exchange notes.

As of March 31, 2011, we had a total of approximately $1,470 million in aggregate principal amount of outstanding indebtedness. This substantial level of indebtedness could have important consequences. For example, it may:

- make it more difficult for us to satisfy our financial obligations, including those relating to the exchange notes;
- require us to dedicate a substantial portion of our cash flow from operations to payments on our indebtedness, thereby reducing the availability of our cash flow to fund working capital, capital expenditures and other general corporate purposes;
- limit our ability to obtain additional financing to expand our business or alleviate liquidity constraints, as a result of financial and other restrictive covenants in our indebtedness;
- limit our ability to refinance all or a portion of our indebtedness on or before maturity;
- limit our ability to pursue our acquisition strategy;
- increase our vulnerability to general adverse economic and industry conditions;
- limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate; and
- place us at a competitive disadvantage relative to companies that have proportionately less indebtedness.

Despite our significant level of debt, we may still be able to incur more debt and take other actions, including making restricted payments, which could intensify the risks described above.

We may be able to incur significant amounts of debt in the future or take other actions that may impair our ability to repay the exchange notes, subject to compliance with our existing debt agreements. Although our senior secured credit facilities, the indentures governing our existing notes and the indenture that will govern the exchange notes contain or will contain restrictions on our incurrence of additional debt, including secured debt, we could still incur substantial debt in compliance with these restrictions. For example, the indenture that will govern the exchange notes will allow us to incur additional debt if our consolidated leverage ratio, after giving effect to the incurrence, is less than 4.75 to 1.0, and to incur additional secured debt if our secured indebtedness leverage ratio, after giving effect to the incurrence, does not exceed 3.25 to 1.0. In addition, under our senior secured credit facilities, we may incur up to approximately $65 million in aggregate principal amount of incremental term loans, subject to conditions, and up to $50 million in aggregate principal amount of revolving loans. Further, the indenture that will govern the exchange notes will permit us to pay dividends on our common stock, repurchase our common stock and make other restricted payments in an amount that is based in part on the amount by which our cumulative Consolidated EBITDA has exceeded and will exceed 140% of our cumulative Consolidated Interest Expense, as defined under the indenture, since October 1, 2010. If we incur additional debt in the future, the related risks that we face would be increased.

Table of Contents

Covenants under the indenture that will govern the exchange notes and under our other debt agreements may restrict our future operations.

Our senior secured credit facilities, the indentures governing our existing notes and the indenture that will govern the exchange notes impose operating and financial restrictions that limit our discretion to take action on some business matters, which could make it more difficult for us to expand, finance our operations and engage in other business activities that may be in our interest. These restrictions include compliance with or maintenance of certain financial tests and ratios, including a maximum consolidated leverage ratio under our credit facilities, which limit our ability and that of our subsidiaries to:

- incur or guarantee additional indebtedness;
- pay dividends on, redeem or repurchase our capital stock;
- make investments or repay subordinated indebtedness;
- engage in sale-leaseback transactions;
- enter into transactions with affiliates;
- sell assets;
- create liens;
- create restrictions on dividend and other payments to us from our subsidiaries;
- issue or sell stock of subsidiaries; and
- engage in a merger or consolidation, or sell, transfer or otherwise dispose of all or substantially all of our assets.

These restrictions may prevent us from taking actions that we believe would be in the best interest of our business and may make it difficult for us successfully to execute our business strategy or effectively compete with companies that are not similarly restricted. We also may incur future debt obligations that might subject us to additional restrictive covenants that could affect our financial and operational flexibility. We may not be granted waivers or amendments under out debt agreements if for any reason we are unable to comply with the agreements, and may not be able to refinance our debt on terms acceptable to us, or at all. The breach of any of the covenants under our senior secured credit facilities, the indentures governing our existing notes or the indenture that will govern the exchange notes could result in a default under these agreements. An event of default under our debt agreements could permit our lenders or other debt holders to declare all amounts borrowed from them to become due and payable immediately.

We may not be able to repay the exchange notes and our other indebtedness if we do not generate sufficient cash from operations or financings.

Our ability to make payments on or to refinance our indebtedness, including the exchange notes, will depend on our ability in the future to generate cash flows from operations, which is subject to all the risks of our business, and to raise additional funds, including through the offering of equity securities or other debt securities. We may not be able to generate sufficient cash flows from operations for us to repay our indebtedness when such indebtedness becomes due and to meet our other cash needs. If we are unable to generate such cash flows, we may be required to adopt one or more alternatives, such as selling assets, restructuring indebtedness or obtaining additional capital on terms that may be burdensome to our company or unfavorable to the holders of the exchange notes. Our ability to refinance our indebtedness will depend on the capital markets and our financial condition at such time and will be limited by the restrictive covenants in our debt agreements. We may not be able to engage in any of these activities or engage in these activities on advantageous terms, which could cause us to default on our exchange notes and our other debt obligations.

Table of Contents

The exchange notes and the subsidiary guarantees will be effectively subordinated in right of payment to our secured debt.

The exchange notes and the subsidiary guarantees will be general, unsecured obligations of PAETEC Holding and the subsidiary guarantors and will be effectively subordinated in right of payment to all of our secured debt, including our existing senior secured credit facilities and the 8 7/8% senior secured notes, to the extent of the value of the assets securing such debt. As of March 31, 2011, we had $675 million of senior secured debt outstanding and would have had the ability to draw up to $25 million in additional principal amount of borrowings under our senior secured revolving credit facility. Immediately after this offering, we will have the ability to incur additional secured debt under our senior secured credit facilities, the indentures governing the existing notes and the indenture that will govern the exchange notes. Substantially all of our assets have been pledged as collateral to secure repayment of our obligations under our senior secured credit facilities and the 8 7/8% senior secured notes. In the event of a bankruptcy, liquidation, dissolution, reorganization or similar proceeding with respect to PAETEC Holding, such assets would be available to satisfy obligations under the secured debt before any payment could be made on the exchange notes. In addition, to the extent such assets were insufficient to satisfy in full our secured debt, the holders of such secured debt would have a claim for any shortfall that would rank equal in right of payment with the exchange notes. Accordingly, there may only be a limited amount of assets available to satisfy your claims as a holder of exchange notes upon any acceleration of payment of the exchange notes upon the occurrence of any such proceeding.

The indenture that will govern the exchange notes permits us to form a holding company that would be permitted to take actions that may not be consistent with the best interests of the holders of the exchange notes.

The indenture that will govern the exchange notes permits us to form a separate holding company that would be the parent company of PAETEC Holding and PAETEC Holding s subsidiaries. If such a holding company were formed, some of the restrictive covenants contained in the indenture would apply only to PAETEC Holding and PAETEC Holding s subsidiaries and not to the new holding company. As a result, the new holding company could take actions, such as using cash for purposes unrelated to debt service, which may not be consistent with your best interests.

We may be unable to repurchase the exchange notes in the event of a change of control of our company.

Upon the occurrence of a change of control (as defined in the indenture that will govern the exchange notes), the holders of the exchange notes will have the right to require us to repurchase their exchange notes at a price equal to 101% of the principal amount of the exchange notes, together with any accrued and unpaid interest, if any, to the date of repurchase. If a change of control occurs, we may not have sufficient funds available to meet our repurchase obligations. Accordingly, we may be unable to pay the holders of the exchange notes the change of control purchase price for their exchange notes. Our failure to pay the change of control purchase price when due would constitute a default under the indenture that will govern the exchange notes and would give the trustee thereunder and the holders of the exchange notes the rights described in Description of the Exchange Notes Events of Default and Remedies.

The holders of our existing notes have the right to require us to repurchase all of their notes at the same repurchase price upon the occurrence of the same change of control event. Under our senior secured credit facilities, a change of control is an event of default that would permit the lenders thereunder to accelerate all amounts outstanding under the facilities. If such indebtedness is not paid, such lenders may enforce their security interests in the collateral securing our secured indebtedness, thereby limiting our ability to raise cash to purchase the exchange notes and reducing the practical benefit to the holders of the exchange notes of the repurchase provisions of the indenture that will govern the exchange notes. In addition, the terms of our senior secured credit facilities prevent us, and the terms of our future indebtedness may prevent us, from paying you if there is a change of control of our company.

Table of Contents

The definition of change of control in the indenture that will govern the exchange notes will include a phrase relating to the sale, conveyance, transfer or lease of all or substantially all of our assets. There is no precise established definition of the phrase substantially all under applicable law. Accordingly, the ability of a holder of the exchange notes to require us to repurchase exchange notes as a result of a sale, conveyance, transfer or lease of less than all of our assets to another person may be uncertain.

Federal and state fraudulent conveyance laws may permit a court to void the exchange notes and the subsidiary guarantees, and, if that occurs, you may not receive any payments on the exchange notes or the subsidiary guarantees.

The issuance of the exchange notes and the subsidiary guarantees may be subject to review under federal and state fraudulent conveyance statutes. Although the relevant laws may vary from state to state, the payment of consideration generally will be a fraudulent conveyance under such laws if:

- it was paid with the intent of hindering, delaying or defrauding creditors; or
- we or any subsidiary guarantor received less than reasonably equivalent value or fair consideration in return for issuing either the exchange notes or a subsidiary guarantee, as applicable, and either:
  - we or the subsidiary guarantor was insolvent or rendered insolvent by reason of the incurrence of the debt;
  - payment of the consideration left us or the subsidiary guarantor with an unreasonably small amount of capital to carry on our or its business; or
  - we or the subsidiary guarantor intended to, or believed that we or it would, incur debts beyond our or its ability to pay the debt.

If a court were to find that the issuance of the exchange notes or a subsidiary guarantee was a fraudulent conveyance, the court could void the payment obligations under the exchange notes or such subsidiary guarantee or subordinate the exchange notes or such subsidiary guarantee in right of payment to existing and future debt, or require the holders of the exchange notes to repay any amounts received with respect to the exchange notes or such subsidiary guarantee. In the event of a finding that a fraudulent conveyance occurred, you may not receive any repayment on the exchange notes, may not have a claim against the subsidiary guarantor and may only be a general unsecured creditor of us or our subsidiary.

The subsidiary guarantees also could be subject to the claim that, because they were incurred for our benefit (and only indirectly for the benefit of the subsidiary guarantors), the obligations of the subsidiary guarantors were incurred for less than reasonably equivalent value or fair consideration. A court could then void a subsidiary guarantor s obligation under its subsidiary guarantee, subordinate the subsidiary guarantee in right of payment to other debt of the subsidiary guarantor or take other action detrimental to your interests as a holder of exchange notes.

We are a holding company and conduct all of our operations exclusively through our subsidiaries. Our only significant assets are the capital stock of our subsidiaries. If the subsidiary guarantees are unenforceable, your interests would be effectively subordinated in right of payment to all of our subsidiaries debt and other liabilities, including liabilities to trade creditors.

There is currently no public market for the exchange notes and an active trading market may not develop for the exchange notes. The failure of a market to develop for the exchange notes could adversely affect the liquidity and value of the exchange notes.

The exchange notes will be a new issue of securities for which there is no established trading market. There can be no assurance that a trading market for the exchange notes will develop or as to the liquidity of any market that may develop. If an active trading market for the exchange notes does not develop, the market price and liquidity of the exchange notes may be adversely affected.

14

The liquidity of any trading market for the exchange notes and future trading prices of the exchange notes will depend on many factors, including, among others, the number of holders of the exchange notes, prevailing interest rates, our operating results, financial performance and prospects, the interest of securities dealers in making a market in the exchange notes, and the market for similar securities and the overall securities market, and may be adversely affected by unfavorable changes in these factors. Historically, the market for non-investment grade debt securities has been subject to disruptions that have caused substantial fluctuations in the prices of such securities. Any trading market for the exchange notes may be subject to similar disruptions, which could adversely affect the value of the exchange notes.

The initial purchasers of the original notes have informed us that they intend to make a market in the exchange notes after this offering is completed. However, the initial purchasers are not obligated to do so and may cease any market-making activities at any time without notice in their sole discretion. We do not intend to apply for a listing of the exchange notes on any national securities exchange or for the inclusion of the exchange notes on any automated dealer quotation system.

Risks Related to Our Business

PAETEC s business and operations are subject to a number of risks and uncertainties, including the following:

Deterioration in the global economy has had, and may continue to have, a negative impact on PAETEC s business.

PAETEC believes that the financial and economic pressures faced by its business customers in the current environment of diminished consumer spending, corporate downsizing and tightened credit have had, and may continue to have, an adverse effect on billable minutes of use and on customer attrition rates. These pressures also have resulted in, and may continue to result in, increased customer demands for price reductions in connection with contract renewals.

If PAETEC cannot continue to interconnect with and obtain key network elements and special access services from some of its primary competitors on acceptable terms, it may not be able to offer its voice and data services on a profitable basis, if at all.

PAETEC will not be able to provide its voice and data services on a profitable basis, if at all, unless it is able to continue to interconnect with and obtain key network elements and special access services from some of PAETEC s primary competitors on acceptable terms. To offer voice and data services in a market, PAETEC must interconnect its network with the network of the incumbent carrier in that market. This relationship is governed by interconnection agreements between the incumbent carrier and PAETEC that are based on provisions of the Telecommunications Act of 1996, or the Telecom Act, obligating incumbent carriers to interconnect with competitive carriers and provide them with access to various elements of the incumbent s network on an unbundled basis at cost-based prices. In February 2011, the Federal Communications Commission, or FCC, asked in a notice of proposed rulemaking whether and how it should encourage carriers to transition to Internet Protocol, or IP, interconnection, and how IP interconnection fits within existing legal and technical frameworks. To the extent that the FCC determines that IP interconnection between PAETEC and incumbent carriers is not governed by the Telecom Act, PAETEC s ability to interconnect and exchange traffic with incumbent carriers on reasonable rates, terms, and conditions could be adversely affected.

Additional changes in law or regulation that limit PAETEC s ability to use key network elements of the incumbent carrier may have an adverse impact on the company s ability to serve its end-user customers. PAETEC must interconnect with and lease from incumbent carriers last mile facilities, which for services offered to PAETEC s business customers, include special access digital T1 transmission lines and unbundled network element, or UNE, digital T1 transmission lines and other elements. To serve the consumer customers of Cavalier that purchase basic telephony services or digital subscriber line services, the last mile facilities include DS0 and 2-wire UNE loops. Access to last mile special access digital T1 transmission lines is governed by each incumbent local exchange carrier s special access tariffs or contract tariffs. These tariffs can be changed and the prices for the services increased. Interconnection agreements can be terminated or expire and thereby require renegotiation and renewal. Current FCC rules permit the regional Bell operating companies, or RBOCs, to retire unilaterally without any regulatory oversight last mile copper loop facilities that PAETEC has used historically to reach its customers and, after its acquisition of Cavalier, now also uses to reach many of its new customers served by DS0 and 2-wire UNE loops. As incumbent carriers replace copper facilities with fiber loop facilities that the FCC has declared are not subject to unbundling obligations for serving consumer and very small business customers, such carriers may be able to eliminate PAETEC s access to last mile facilities that it requires. Several competitive broadband carriers, including PAETEC, have petitioned the FCC to change the rules governing copper loop retirement to protect access to these last mile facilities, but the FCC has not yet made any decision on the petition.

Revised FCC policy or rules governing intercarrier compensation could have a material adverse effect on PAETEC s operating results.

Adoption of significant changes in policy or rules governing intercarrier compensation by the FCC and the time frame over which changes are to be implemented could have a material adverse effect on PAETEC s collection and payment of reciprocal compensation and access fees. Intercarrier compensation, including exchange access and reciprocal compensation, currently is the subject of several ongoing proceedings before the FCC that are intended to reform the way in which carriers and service providers pay other carriers and providers for the use of their respective networks. In February 2011, the FCC issued a notice of proposed rulemaking in which it proposed some initial changes to the rules governing intercarrier compensation, and more generally proposed significant reforms to intercarrier compensation over a number of years. The initial proposed reforms would clarify specific calling party information that all service providers are to attach to traffic to ensure that all existing traffic may be billed and to clarify the applicable intercarrier compensation rate for interconnected VoIP traffic. In addition, the FCC proposed rules to reduce access rates a service provider may charge when it chooses to directly or indirectly share access revenues with a third party that causes a large amount of traffic to originate or terminate through that service provider s network. The FCC has proposed in the long term to reduce or eliminate intercarrier compensation and requested comment on the timing, speed, and sequencing of how to reduce current rates for categories of traffic that are subject to different compensation rates today. Given the breadth of questions on which the FCC seeks comment, there is no clear indication as to how the FCC will modify rules governing intercarrier compensation.

PAETEC s business is subject to a variety of risks based on its dependence on regulations that continue to change.

Most of the network services and carrier services that PAETEC provides are subject to regulation and may be adversely affected by regulatory developments at the federal, state and local levels. For example, the regulations can affect the types of services PAETEC may offer, the rates PAETEC is permitted to charge for its services and for the use of its network by other carriers, the manner in which PAETEC may bill its customers and the rates PAETEC must pay others for their services and for the use of their networks. Services offered to residential customers and small business customers typically are subject to more extensive regulation than services offered to medium-sized and large business customers, and some sales techniques such as telemarketing typically used to market services to consumers and very small business customers are subject to regulations that do not apply to service provided through direct or agent sales channels. In addition, the regulations may impose specific operational or compliance requirements related to the protection of customer proprietary network information, capability to associate a physical address with a calling party s telephone number, or cooperation with law enforcement officials engaged in lawful communication interception or monitoring activities. All of these requirements may reduce the revenue PAETEC generates from its operating activities or increase its operating costs. Federal and state regulations also determine the level of contribution payments PAETEC must make to the federal Universal Service Fund and other federal and state telecommunications subsidy programs, as well as the terms under which it may use any rights-of-way necessary for the operation of its business. If PAETEC fails to comply with applicable regulations, or if the regulations change in a manner adverse to PAETEC, its business and operating results may suffer.

If PAETEC is required to reduce the prices it charges for some or all of its network services, PAETEC s profitability may be negatively affected and its ability to continue to generate positive cash flows from operations may be diminished.

PAETEC may be required to reduce the prices it charges for some or all of its network services, which could adversely affect its profit margins and its ability to generate positive cash flows from operations, for the following reasons:

- the incumbent carriers in the markets PAETEC serves already offer a bundle of local, long distance and data services that is the same as or similar to, and in some cases more robust than, the bundle of services that PAETEC offers;

- PAETEC s current and potential customers are increasingly using Voice over Internet Protocol, or VoIP, which could reduce or eliminate long distance revenues generated by those customers;

- Cavalier s residential service offering competes with consumer wireless services and providers such as Vonage Holdings Corp., magicjack, LP, Google Inc., Skype Inc. and cable companies that use IP technology, all of which offer services using either their private IP networks or the public Internet to access their customers;

- the mergers between AT&T Inc. and SBC Communications, Inc., between MCI, Inc. and Verizon Communications Inc., and between AT&T and BellSouth Corporation, as well as the proposed merger between CenturyLink, Inc. and Qwest Corporation, provide, or are expected to provide, these carriers with significant operating efficiencies and substantially greater marketing, financial and technical resources as they compete with PAETEC;

- regulatory authorities generally have decreased their oversight of incumbent carriers, including wholesale obligations of these carriers, and from time to time are asked to forbear from applying a range of regulations to incumbent carriers, which may increase the benefits these companies obtain from their longstanding customer relationships and facilitate their ability to reduce prices for local and other network services by offsetting those reductions with revenue or profits generated by unrelated businesses, products or services;

- states, or the FCC, if it elects to preempt state jurisdiction, may impose limits on intrastate access rate levels that competitive carriers such as PAETEC may charge interexchange carriers when providing switched access services on intrastate long distance traffic; and

- regulatory authorities have permitted incumbent carriers to exercise pricing flexibility in setting the rates they charge for some of the network services that PAETEC also provides, rather than requiring these incumbent carriers to charge set rates.

Industry consolidation and realignment may increase PAETEC s costs.

Before their respective mergers, AT&T and MCI offered some network services and elements in competition with the incumbent carriers, including high-speed circuits (DS1 and DS3 and OCN), interoffice transport and last mile access loops to some premises. The mergers between AT&T and SBC and between AT&T and BellSouth have increased the cost of the high-speed circuits that PAETEC leases to connect its customers to PAETEC s switching equipment. The merger between MCI and Verizon also could increase the cost of similar high-speed circuits in the Verizon region by reducing the number of providers that offer those high-speed

circuits. PAETEC also may incur increased circuit costs in portions of the Qwest region, where these large incumbents may not have a significant presence. Such a development could decrease the competitive pressure on other carriers to maintain low rates for these circuits. The expansion of operations of medium-sized incumbent carriers into markets served by PAETEC, either through merger or the sale of exchanges by an RBOC to a smaller incumbent carrier, may negatively affect PAETEC s operations if the non-RBOC incumbent carrier has less sophisticated systems and more costly terms for interconnection and access to last mile facilities. As a result of its proposed acquisition of Qwest announced in April 2010, CenturyLink will become the incumbent local exchange carrier in the existing Qwest 14-state region. In its filings to secure regulatory approval of the transaction, CenturyLink has not agreed to use the legacy Qwest operational support systems after 30 months following the transaction closing date. If CenturyLink subsequently attempts to change the existing Qwest operational support systems to significantly less advanced systems, such a change would negatively affect PAETEC s ability to serve its existing customers and obtain new customers, and would increase PAETEC s operating costs.

PAETEC s operating performance will suffer if it is not offered competitive rates for the access services PAETEC needs to provide its long distance services.

PAETEC depends on other telecommunications companies to originate and terminate a significant portion of the long distance traffic initiated by PAETEC s network services customers. Access charges historically have made up a significant percentage of the overall cost associated with the provision of long distance service by PAETEC. If the volume of long distance traffic PAETEC carries remains substantial, its operating performance will suffer if it is not offered these access services at rates that are substantially equivalent to the rates charged to its competitors or that otherwise do not enable it to have profitable pricing of its long distance services.

PAETEC s customer churn rate may increase, which could have an adverse effect on PAETEC s revenues.

Higher customer churn, or attrition, rates could adversely impact PAETEC s revenue growth, while a sustained or significant growth in the churn rate could have a material adverse effect on PAETEC s financial condition. Customer churn occurs when a customer discontinues service with PAETEC either voluntarily, such as when a customer switches to a competitor, or involuntarily, such as when a customer goes out of business. Changes in the economy, increased competition from other providers, the types of customers PAETEC serves, or issues with PAETEC s service quality could increase the company s customer churn rate. PAETEC anticipates that lower prices offered by PAETEC s competitors may contribute to greater customer churn. In addition, the churn rate may increase because the rate of attrition of small business and residential customers, many of which PAETEC acquired through its acquisition of Cavalier, is traditionally higher than the attrition rate for larger enterprise customers.

If PAETEC does not compete effectively in the highly competitive market for network services, it could lose customers and revenue and may face more difficulties as it expands in existing markets and enters new markets.

The telecommunications industry is highly competitive, particularly with the advent of new technologies replacing traditional public switched telecommunications networks in favor of services transmitted over the Internet. This increased level of competition could diminish PAETEC s market share and affect PAETEC s ability to expand PAETEC s business. PAETEC will compete with current and potential market entrants, including:

- AT&T, Qwest, Verizon and CenturyLink, which are the large, former monopoly local telephone companies and their successors;
- other competitive carriers, competitive access providers, Internet service providers and stand-alone VoIP providers; and
- for consumer services offered by Cavalier, wireless services providers such as Vonage, magicjack, Google and Skype, and cable companies.

Table of Contents

Many of the competitors identified above have significantly greater market presence, engineering and marketing capabilities, and financial, technological and personnel resources than PAETEC. Additionally, some of these competitors are currently subject to substantially less regulation than competitive and incumbent carriers and claim to be exempt from a number of taxes and regulatory charges that PAETEC is required to pay. As a result, PAETEC s competitors may be able to develop and expand their network infrastructures and service offerings more efficiently or more quickly, adapt more swiftly to new or emerging technologies and changes in customer requirements, take advantage of acquisitions and other opportunities more readily, and devote greater resources to the marketing and sale of their products and services than PAETEC.

Changes in technology, service offerings and customer preferences could affect PAETEC s ability to compete in the marketplace for telecommunications and information services.

PAETEC faces rapid and significant changes in technology. PAETEC s ability to retain existing customers and attract new customers will be impaired if PAETEC is unable to deliver new technologies and services that have significant customer acceptance, to adopt those new technologies and offer those new services in a timely and effective manner, and to compete successfully against other service providers that introduce the same or similar new technologies and offer substantially similar new services. The telecommunications industry has changed significantly over the past several years and is continuing to evolve rapidly. Emerging technologies and services, such as VoIP applications, broadband services and advanced wireless offerings, are altering the economic conditions under which the telecommunications and information services industry operates. New technologies also could lead to the development of new, more convenient and cost-effective services. In addition, the preferences and requirements of customers are rapidly changing. For example, telecommunications customers are increasingly using wireless forms of communication, such as handheld Internet-access devices and mobile phones. The use of wireless communications has resulted in a decline in the volume of voice traffic carried by traditional wireline telecommunications networks and likely has resulted in a decrease in the average minutes of use generated by customers of wireline communications services providers, including PAETEC. In addition, a significant percentage of residential customers in the United States have stopped subscribing to any landline telephone service and rely exclusively on wireless services, which PAETEC currently does not offer. PAETEC expects these trends to continue.

The development and offering of new services in response to new technologies or consumer demands may require PAETEC to increase its capital expenditures significantly. For instance, PAETEC may be required to convert its existing network to a network using more advanced technology. If PAETEC is unable successfully to install or operate new network equipment or convert its network, or if the technology choices PAETEC makes prove to be incorrect, ineffective or unacceptably costly, PAETEC may not be able to compete effectively. In addition, new technologies may be protected by patents or other intellectual property laws, and, therefore, may be available only to PAETEC s competitors.

If PAETEC does not successfully implement its acquisition strategy, its acquisition of other businesses could harm PAETEC s results of operations and financial condition.

As part of PAETEC s growth strategy, PAETEC seeks to supplement internal expansion through targeted acquisitions. PAETEC is subject to various risks in connection with any acquisitions or series of acquisitions, including the risks that PAETEC:

- may be unable to realize anticipated cost savings or operating efficiencies, to retain skilled management, technical, sales and back office personnel of acquired companies, to maintain uniform standards, controls, procedures and policies throughout all of its acquired companies, or to manage successfully the risks associated with its entry into new geographical, customer or product markets in which it has little or no experience;

- may suffer adverse developments in its relationships with vendors, face brand awareness issues related to the acquired assets or customers, be forced to limit the attention it can devote to any one acquired company, and suffer disruption of its ongoing business operations as a result of its acquisition and integration activities;

may encounter resistance by customers of acquired companies to PAETEC s marketing programs, pricing levels or services and may not successfully incorporate the services of acquired businesses into PAETEC s package of service offerings or successfully integrate the network equipment, billing and operating support systems of acquired businesses; and

may experience difficulties in evaluating the historical or future financial performance of the acquired companies.

Even if acquired companies eventually contribute to an improvement in PAETEC s operating results or financial condition, the acquisitions may adversely affect PAETEC s operating results and financial condition in the short term. PAETEC s operating results may decrease as a result of transaction-related expenses PAETEC records for the period in which it completes an acquisition. PAETEC s operating results may be further reduced by the higher operating and administrative expenses PAETEC may incur in the periods immediately following an acquisition as PAETEC integrates the acquired business into its operations.

Any significant impairment of PAETEC s goodwill would lead to a decrease in PAETEC s assets and a reduction in its net operating performance.

At March 31, 2011, PAETEC had goodwill of approximately $443.8 million, which constituted approximately 22.1% of PAETEC s total assets at that date. If PAETEC makes changes in its business strategy or if market or other conditions adversely affect its business operations, PAETEC may be forced to record an impairment charge, which would lead to a decrease in the company s assets and reduction in net operating performance. For 2008, PAETEC recorded a goodwill impairment charge of $355.0 million. PAETEC tests goodwill for impairment annually or whenever events or changes in circumstances indicate an impairment may have occurred. If the testing performed indicates that impairment has occurred, PAETEC is required to record an impairment change for the difference between the carrying value of the goodwill and the implied fair value of the goodwill in the period in which the determination is made. The testing of goodwill for impairment requires PAETEC to make significant estimates about the future performance and cash flows of the company, as well as other assumptions. These estimates can be affected by numerous factors, including changes in economic, industry or market conditions, changes in underlying business operations, future reporting unit operating performance, existing or new product market acceptance, changes in competition, or changes in technologies. Any changes in key assumptions, or actual performance compared with those assumptions, about PAETEC s business and its future prospects or other assumptions could affect the fair value of one or more reporting units, and result in an impairment charge.

Adverse developments in the credit and capital markets may negatively affect PAETEC s ability to raise additional capital.

Adverse conditions in the debt security and syndicated loan markets, which have significantly reduced the availability of corporate credit, are continuing to affect the global financial system and equity markets. PAETEC s ability to access the debt and equity markets may be restricted at a time when it would like, or need, to access such markets. Such reduced access could have an adverse effect on PAETEC s flexibility to react to changing economic and business conditions. Further, the disruptions in the financial markets have had, and may continue to have, an adverse effect on the market value of PAETEC s common stock, which could make it more difficult or costly for the company to raise capital through an offering of its equity securities.

If PAETEC is unable to raise additional capital, its ability to expand its business and to meet its obligations will be limited.

The development and expansion of PAETEC s network will require substantial capital investment. If PAETEC chooses to accelerate the expansion of its business, PAETEC will require additional capital. PAETEC also may require additional capital to fund payments of its indebtedness as an increasing amount of such

Table of Contents

indebtedness becomes due and payable. If PAETEC cannot successfully obtain additional equity or debt financing for necessary purposes on acceptable terms, PAETEC could be at a competitive disadvantage relative to competitors with significant capital or the ability to raise significant capital for expansion. The terms of any financing PAETEC does obtain may be burdensome to PAETEC.

If PAETEC does not continue to attract and retain qualified personnel and independent sales agents or retain its key management, PAETEC may not be able to execute its business plan.

PAETEC faces competition for qualified personnel, including management, technical and sales personnel. PAETEC also relies on a large number of independent sales agents to market and sell PAETEC s services. If PAETEC is unable to attract and retain experienced and motivated personnel, including a large and effective direct sales force, a substantial number of independent sales agents, and qualified information technology and other back office personnel, PAETEC may not be able to obtain new customers or effectively service existing customers, or sell sufficient amounts of service to execute PAETEC s business plan. Additionally, the loss of key management personnel could impair PAETEC s ability to implement its acquisition integration plan and execute its business strategy, which could hinder PAETEC s ability to sustain profitable operations.

Failure to obtain and maintain necessary permits and rights-of-way could interfere with PAETEC s network infrastructure and operations.

To obtain and maintain rights-of-way and similar rights and easements needed to install, operate and maintain fiber optic cable and its other network elements, PAETEC must negotiate and manage agreements with state highway authorities, local governments, transit authorities, local telephone companies and other utilities, railroads, long distance carriers and other parties. The failure to obtain or maintain any rights-of-way could interfere with PAETEC s operations, interfere with its network infrastructure and adversely affect PAETEC s business. For example, if PAETEC loses access to a right-of-way, it may need to spend significant sums to remove and relocate its facilities.

PAETEC and other industry participants are frequently involved in disputes over issues that, if decided adversely to PAETEC, could harm PAETEC s financial and operational prospects.

PAETEC anticipates that it will continue to be subject to risks associated with the resolution of various disputes, lawsuits, arbitrations and proceedings affecting PAETEC s business. The deregulation of the telecommunications industry, the implementation of the Telecom Act, the evolution of telecommunications infrastructure from time-division multiplexing to Internet Protocol, and the financial distress of many carriers in the telecommunications industry as a result of continued competitive factors and financial pressures have resulted in the involvement of numerous industry participants, including PAETEC, in disputes, lawsuits, proceedings and arbitrations before state and federal regulatory commissions, private arbitration organizations such as the American Arbitration Association, and courts over many issues that will be important to PAETEC s financial and operational success. These issues include the interpretation and enforcement of existing interconnection agreements and tariffs, the terms of new interconnection agreements, operating performance obligations, intercarrier compensation, treatment of different categories of traffic (for example, traffic originated or terminated on wireless networks or VoIP), the jurisdiction of traffic for intercarrier compensation purposes, the wholesale services and facilities available to PAETEC, the prices PAETEC will pay for those services and facilities, and the regulatory treatment of new technologies and services.

PAETEC s business could suffer if third parties successfully claim that PAETEC has infringed their intellectual property rights.

The dependence of the telecommunications industry on proprietary technology has resulted in increasingly frequent litigation based on allegations of the infringement of patents and other intellectual property. PAETEC may be subject to litigation to defend against claimed infringement of the rights of others or to determine the scope and validity of the proprietary rights of others. Regardless of its merits, any intellectual property litigation could be time-consuming and costly and could divert management s time and attention from PAETEC s business operations.

Table of Contents

If PAETEC is unable to maintain or enhance its back office information systems, PAETEC may not be able to increase its revenue as planned or to compete effectively.

Sophisticated back office information systems are vital to PAETEC s revenue growth and PAETEC s ability to monitor costs, bill customers, initiate, implement and track customer orders, and achieve operating efficiencies. To increase revenue, PAETEC must select products and services offered by third-party vendors and efficiently integrate those products and services into PAETEC s existing back office operations. PAETEC may not successfully implement these products, services and systems on a timely basis, and PAETEC s systems may fail to perform as the company expects. A failure or delay in the expected performance of PAETEC s back office systems, or a failure or delay in effectively integrating the back office systems of acquired companies with PAETEC s back office systems, could slow the pace of PAETEC s expected revenue growth or harm PAETEC s competitiveness by adversely affecting PAETEC s service quality, which could lead to a loss of existing customers or a failure to attract and retain new customers. PAETEC s business could suffer similar harm if incumbent local exchange carriers are permitted under applicable regulation to modify or degrade substantially any existing operational support systems that are used by PAETEC s back office systems to order network elements or other services, correct service problems, and bill customers.

Network failures or system breaches could cause delays or adversely affect PAETEC s service quality, which may cause it to lose customers and revenue.

In operating its network, PAETEC must maintain connections for, and manage, a large number of customers and a large quantity of traffic at high speeds. Any failure or perceived failure to achieve or maintain high-speed data transmission could significantly reduce demand for PAETEC s services and adversely affect PAETEC s operating results. In the past, PAETEC has experienced outages, such as temporary switch outages, that have prevented it from providing uninterrupted services to some of its customers. Such outages have resulted in lost revenue and could cause PAETEC to lose customers. In the future, PAETEC may experience similar or more severe outages or other network failures or breaches. Computer viruses, break-ins, human error, natural disasters and other problems also may disrupt PAETEC s network. The network security and stability measures PAETEC implements may be circumvented in the future or otherwise fail to prevent the disruption of PAETEC s services. The costs and resources required to eliminate computer viruses and other security problems may result in interruptions, delays or cessation of services to PAETEC s customers, which could result in reduced demand for PAETEC s services, decrease PAETEC s revenue and slow PAETEC s planned expansion.

If PAETEC s network or other ground facilities are damaged by natural catastrophes or terrorism, PAETEC s ability to provide services may be interrupted and the quality of PAETEC s services may be adversely affected.

A major earthquake, hurricane, tornado, fire, terrorist attack on the United States, or other catastrophic event could damage PAETEC s network, network operations centers, central offices or corporate headquarters. Such an event could interrupt PAETEC s services, adversely affect service quality and harm PAETEC s business. PAETEC does not have replacement or redundant facilities that it can use to provide alternative means of service to all customers or under every circumstance in the event of a catastrophic event. Any damage to PAETEC s network could result in degradation of PAETEC s service for some customers and could result in complete loss of service in affected areas.

Future sales of PAETEC s common stock in the public market could lower the price of PAETEC common stock and impair PAETEC s ability to raise funds in future securities offerings.

Future sales of a substantial number of shares of PAETEC common stock in the public market, or the perception that such sales could occur, could adversely affect the prevailing market price of PAETEC common stock and could make it more difficult for PAETEC to raise funds through a public offering of its equity securities. PAETEC stockholders with rights under existing registration rights agreements will have the benefit, subject to limitations and qualifications, to registration rights with respect to their PAETEC common stock that would permit the sale of such common stock in the public market.

Table of Contents

If PAETEC fails to maintain proper and effective internal control over financial reporting or fails to implement any required changes, PAETEC s ability to produce accurate financial statements could be impaired, which could increase its operating costs and adversely affect its ability to operate its business.

PAETEC is required to provide annual management assessments of the effectiveness of its internal control over financial reporting and to provide reports by PAETEC s independent registered public accounting firm addressing the effectiveness of internal control over financial reporting. Ensuring that PAETEC has adequate internal control over financial reporting so that PAETEC can produce accurate financial statements on a timely basis is a costly and time-consuming effort. Implementing any required changes to PAETEC s internal controls may require modifications to PAETEC s existing accounting systems or the engagement of additional accounting personnel. Any failure to maintain adequate internal controls, or the inability to produce accurate financial statements on a timely basis, could increase PAETEC s operating costs and impair PAETEC s ability to operate its business.

Table of Contents

FORWARD-LOOKING STATEMENTS

Some of the statements included in this prospectus constitute forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended, or Exchange Act. These statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, financial position, levels of activity, performance or achievements to be materially different from any future results, financial position, levels of activity, performance or achievements expressed or implied by such forward-looking statements. In some cases, you can identify these statements by forward-looking words such as anticipate, believe, could, estimate, expect, intend, may, plan, potential, should, will and would, or similar words. You should read statements that contain carefully because they discuss our expectations concerning our future results of operations or financial position, or state other forward-looking information. There may be events in the future, however, that we are not able to control or predict accurately. The risks described in the section entitled Risk Factors in this prospectus and in the other information included in this prospectus provide examples of risks, uncertainties and events that may cause our actual results to differ materially from the expectations that we describe in the forward-looking statements. The occurrence of the events described in such risks and other information could have a material adverse effect on our business, results of operations and financial position and could materially adversely affect our ability to meet our obligations under the exchange notes.

We cannot guarantee future results, levels of activity, performance or achievements. You should not place undue reliance on the forward-looking statements included in this prospectus, which apply only as of the date as of which such statements are made. Except as required by law, we expressly disclaim any duty to update the forward-looking statements, and the estimates and assumptions associated with them, after the date as of which such statements are made, whether to reflect changes in circumstances or our expectations, the occurrence of unanticipated events, or otherwise.

Table of Contents

USE OF PROCEEDS

We will not receive any cash proceeds from the issuance of the exchange notes in the exchange offer. In consideration for issuing the exchange notes, we will receive in exchange the original notes in the same principal amount. The terms of the exchange notes will be substantially identical to the terms of the original notes, except that the transfer restrictions, registration rights and related additional interest terms applicable to the original notes will not apply to the exchange notes. The original notes surrendered in exchange for the exchange notes will be retired and canceled and may not be reissued. Accordingly, issuance of the exchange notes will not result in any increase in our outstanding indebtedness or in the obligations of the guarantors of the notes.

Table of Contents

RATIO OF EARNINGS TO FIXED CHARGES

The following table sets forth our consolidated ratios of earnings to fixed charges for the periods indicated.

Year Ended December 31,					Three Months Ended March 31,	
2006	2007	2008	2009	2010	2010	2011
1.58	1.27	(1)	(1)	(1)	(1)	(1)

(1) Earnings were insufficient to cover fixed charges by $398.1 million for the year ended December 31, 2008, $30.0 million for the year ended December 31, 2009, $58.7 million for the year ended December 31, 2010, $10.5 million for the three months ended March 31, 2010 and $11.3 million for the three months ended March 31, 2011. As a result, the ratio of earnings to fixed charges was less than 1.0 for each of such periods.

For purposes of calculating the ratio of earnings to fixed charges for each period, earnings consists of the sum of pre-tax income (loss) from continuing operations, fixed charges, and amortization of capitalized interest, all less capitalized interest. Fixed charges for each period consist of the sum of interest expensed and capitalized, amortized premiums, discounts and capitalized expenses related to indebtedness and the estimated portion of rental expense deemed by us to be representative of the interest factor of rental payments under operating leases.

Table of Contents

SELECTED HISTORICAL CONSOLIDATED FINANCIAL AND OPERATING DATA

The selected consolidated statements of operations data, consolidated balance sheet data, other financial data and operating data reflect the financial results of PAETEC Corp., as predecessor to PAETEC Holding, and PAETEC Corp. s wholly-owned subsidiaries. After February 28, 2007, the date of completion of the merger transaction with US LEC Corp., or US LEC, the accompanying selected data include the accounts of PAETEC Holding and its wholly-owned subsidiaries, including PAETEC Corp. and PAETEC Corp. s wholly-owned subsidiaries and US LEC and US LEC s wholly-owned subsidiaries. After February 8, 2008, the date of completion of the merger transaction with McLeodUSA Incorporated, or McLeodUSA, the accompanying selected data include the foregoing accounts as well as the accounts of McLeodUSA and McLeodUSA s wholly-owned subsidiaries. As of December 6, 2010, the date of completion of the merger transaction with Cavalier, the accompanying selected data include the foregoing accounts as well as the accounts of Cavalier and Cavalier s wholly-owned subsidiaries.

The following tables show the selected consolidated statements of operations data, consolidated balance sheet data, other financial data and operating data of PAETEC Corp. as of and for the year ended December 31, 2006 and of PAETEC Holding as of and for the years ended December 31, 2007, 2008, 2009, and 2010. The selected consolidated statements of operations data and other financial data for the years ended December 31, 2008, 2009 and 2010 and the selected consolidated balance sheet data as of December 31, 2009 and 2010 are derived from PAETEC s audited consolidated financial statements prepared in accordance with generally accepted accounting principles in the United States of America, or GAAP, as included in this prospectus. The selected consolidated statements of operations data and other financial data for the years ended December 31, 2006 and 2007 and the selected consolidated balance sheet data as of December 31, 2006, 2007 and 2008 are derived from PAETEC s audited consolidated financial statements prepared in accordance with GAAP, which are not included or incorporated by reference in this prospectus. The summary financial data as of March 31, 2010 and March 31, 2011 and for the three months ended March 31, 2010 and 2011 are unaudited, but include, in the opinion of our management, all adjustments, consisting of normal, recurring adjustments, necessary for a fair presentation of such data. Our historical results are not necessarily indicative of our results for any future period.

You should read the data set forth below together with the section entitled Management s Discussion and Analysis of Financial Condition and Results of Operations and PAETEC s consolidated financial statements and the related notes thereto included in this prospectus, as well as together with the other financial information included in this prospectus.

	Year Ended December 31,					Three Months Ended March 31,	
	2006	2007[(1)]	2008[(2)]	2009	2010[(3)]	2010	2011
	(in thousands, except per share data)						
Consolidated Statements of Operations Data:							
Revenue:							
Network services revenue	$ 460,347	$ 855,833	$ 1,237,668	$ 1,258,489	$ 1,245,157	$ 310,474	$ 377,032
Carrier services revenue	88,284	144,924	271,279	260,023	262,749	63,043	82,212
Integrated solutions revenue	37,671	40,256	61,433	61,675	115,910	16,534	36,269
Total revenue	586,302	1,041,013	1,570,380	1,580,187	1,623,816	390,051	495,513
Cost of sales (exclusive of operating items shown separately below)	282,169	491,684	781,347	782,389	808,892	192,749	233,912
Selling, general and administrative expenses (exclusive of operating items shown separately below and inclusive of stock-based compensation)	219,516	373,715	572,180	559,541	559,673	134,260	172,692
Leveraged recapitalization related costs	15,153						
Litigation settlement	1,500						
Acquisition, integration and separation costs		3,665	12,700		14,124		2,493
Impairment charge			355,000				
Sales and use tax settlement				(7,221)			
Depreciation and amortization	34,618	75,237	174,251	184,588	196,543	47,173	63,313

Table of Contents

	Year Ended December 31,					Three Months Ended March 31,	
	2006	2007(1)	2008(2)	2009	2010(3)	2010	2011
	(in thousands, except per share data)						
Income (loss) from operations	33,346	96,712	(325,098)	60,890	44,584	15,869	23,103
Debt extinguishment and related costs	5,081	14,558		17,891	7,382	4,423	
Other income, net	(4,509)	(4,784)	(663)	(1,107)	(392)	(112)	(81)
Interest expense	27,319	68,373	73,663	74,149	96,339	22,037	34,464
Change in fair value of Series A convertible redeemable preferred stock conversion right	(10,778)						
Income (loss) before income taxes	16,233	18,565	(398,098)	(30,043)	(58,745)	(10,479)	(11,280)
Provision for (benefit from) income taxes	8,430	8,037	89,797	(1,354)	(1,004)	(941)	650
Net income (loss)	$ 7,803	$ 10,528	$ (487,895)	$ (28,689)	$ (57,741)	$ (9,538)	$ (11,930)
(Loss) income allocated to common stockholders(4)	$ (33,155)	$ 10,528	$ (487,895)	$ (28,689)	$ (57,741)	$ (9,538)	$ (11,930)
Basic net (loss) income per common share(4)	$ (1.05)	$ 0.12	$ (3.48)	$ (0.20)	$ (0.40)	$ (0.07)	$ (0.08)
Diluted net (loss) income per common share(4)(5)	$ (1.05)	$ 0.10	$ (3.48)	$ (0.20)	$ (0.40)	$ (0.07)	$ (0.08)

	As of December 31,					As of March 31,
	2006	2007(1)	2008(2)	2009	2010(3)	2011
	(in thousands)					
Consolidated Balance Sheet Data:						
Cash and cash equivalents	$ 46,885	$ 112,601	$ 164,528	$ 152,888	$ 95,533	$ 103,853
Property and equipment, net	167,566	312,032	638,941	619,048	860,782	863,748
Total assets	379,740	1,166,356	1,496,520	1,457,580	2,007,938	2,008,342
Long-term debt and capital lease obligations (including current portion and net of debt discount)	373,786	795,557	930,833	926,057	1,448,089	1,447,137

	Year Ended December 31,					Three Months Ended March 31,	
	2006	2007(1)	2008(2)	2009	2010(3)	2010	2011
	(in thousands)						
Other Financial Data:							
Net cash (used in) provided by financing activities	(8,202)	290,275	127,767	(44,061)	438,771	18,561	(3,034)
Net cash provided by operating activities	53,555	113,116	152,131	152,169	125,768	7,828	60,685
Net cash used in investing activities	(47,862)	(337,675)	(227,971)	(119,748)	(621,894)	(34,997)	(49,331)
Adjusted EBITDA(6)	91,798	196,178	237,725	256,933	264,931	65,543	91,355

	As of December 31,					As of March 31,	
	2006	2007(1)	2008(2)	2009	2010(3)	2010	2011
Operating Data:							
Geographic markets served(7)	29	53	80	84	86	84	86
Number of switches deployed(8)	13	65	118	122	166	122	166
Total employees	1,312	2,432	3,685	3,693	4,639	3,646	4,507

(1) Includes results of US LEC after the US LEC merger closing date of February 28, 2007.

(2) Includes results of McLeodUSA after the McLeodUSA merger closing date of February 8, 2008.

(3) Includes results of Cavalier as of the Cavalier merger closing date of December 6, 2010.

(4) Basic and diluted net (loss) income per common share for the year ended December 31, 2006 was calculated using the two-class method in accordance with Accounting Standards Codification, or ASC, Topic 260, *Earnings Per Share,* by dividing undistributed (loss) income allocated to common stockholders by the weighted average number of common shares and potential common shares outstanding during the period, after giving effect to the participating security, which was PAETEC Corp. s convertible redeemable preferred stock that was outstanding during the period. During the second

quarter of 2006, as part of a leveraged recapitalization, PAETEC Corp. converted or repurchased all of its outstanding preferred stock. At and after June 30, 2006, there were no participating securities outstanding and, therefore, the two-class method of calculating basic and diluted (loss) income per share does not apply to those periods.

(5) Potential common shares, which under the treasury stock method consist of stock options, warrants, and restricted stock units, and preferred stock assuming the full conversion of such preferred stock, are excluded from the diluted net loss per common share calculations for the years ended December 31, 2006, 2008, 2009 and 2010 and for the three months ended March 31, 2010 and 2011 because the effect of their inclusion would have been anti-dilutive. At December 31, 2006, and thereafter, there were no shares of convertible redeemable preferred stock outstanding.

Table of Contents

(6) Adjusted EBITDA is not a financial measurement prepared in accordance with GAAP. See Management s Discussion and Analysis of Financial Condition and Results of Operations Overview Adjusted EBITDA Presentation for PAETEC s reasons for including adjusted EBITDA data in this prospectus and for material limitations with respect to the usefulness of this measurement. The following table sets forth, for the periods indicated, a reconciliation of adjusted EBITDA to net income (loss), as net income (loss) is calculated in accordance with GAAP:

	Year Ended December 31,					Three Months Ended March 31,	
	2006	2007[1]	2008[2]	2009	2010[3]	2010	2011
	(in thousands)						
Net income (loss)	$ 7,803	$ 10,528	$ (487,895)	$ (28,689)	$ (57,741)	$ (9,538)	$ (11,930)
Add back non-EBITDA items included in net income (loss):							
Depreciation and amortization	34,618	75,237	174,251	184,588	196,543	47,173	63,313
Interest expense, net of interest income	24,995	63,607	71,857	73,188	95,911	21,964	34,413
Provision for (benefit from) income taxes	8,430	8,037	89,797	(1,354)	(1,004)	(941)	650
EBITDA	75,846	157,409	(151,990)	227,733	233,709	58,658	86,446
Stock-based compensation	6,496	20,546	22,015	18,772	9,716	2,462	2,416
Leveraged recapitalization related costs	15,153						
Change in fair value of Series A convertible redeemable preferred stock conversion right	(10,778)						
Debt extinguishment and related costs	5,081	14,558		17,891	7,382	4,423	
Acquisition, integration and separation costs		3,665	12,700		14,124		2,493
Impairment charge			355,000				
Sales and use tax settlement				(7,221)			
Gain on non-monetary transaction				(242)			
Adjusted EBITDA	$ 91,798	$ 196,178	$ 237,725	$ 256,933	$ 264,931	$ 65,543	$ 91,355

(7) Each market represents a geographic area within one of the top 100 U.S. metropolitan statistical areas in which PAETEC offers its network services.

(8) Switches are computers that connect customers to PAETEC s network and transmit voice and data communications over the network.

29

Table of Contents

UNAUDITED PRO FORMA CONDENSED COMBINED FINANCIAL INFORMATION

The following unaudited pro forma condensed combined statement of operations has been prepared to reflect:

the effect of PAETEC s $300 million senior secured notes offering and related debt refinancing completed on January 12, 2010;

the effect of PAETEC s $450 million senior notes offering completed on December 2, 2010 and the application of the proceeds therefrom, together with the cash on hand of PAETEC and Cavalier Telephone Corporation, or Cavalier, to pay the merger consideration and other costs and expenses related to PAETEC s acquisition of Cavalier by merger on December 6, 2010, including repayment of substantially all outstanding Cavalier indebtedness; and

PAETEC s acquisition of Cavalier by merger on December 6, 2010.

You should read this unaudited pro forma condensed combined statement of operations in conjunction with the:

accompanying notes to the unaudited pro forma condensed combined statement of operations; and

separate audited historical consolidated financial statements of PAETEC as of and for the year ended December 31, 2010 and related notes as included in PAETEC s Annual Report on Form 10-K for the year ended December 31, 2010 and incorporated by reference in this prospectus.

The historical financial information of PAETEC for the year ended December 31, 2010 presented in the unaudited pro forma condensed combined statement of operations is derived from the audited consolidated financial statements of PAETEC and the unaudited historical consolidated financial information of Cavalier for the period from January 1, 2010 through December 6, 2010, respectively, but does not include all disclosures required by United States generally accepted accounting principles, or GAAP.

The unaudited pro forma condensed combined statement of operations is provided for informational purposes only. The pro forma information is not necessarily indicative of what the combined companies results of operations actually would have been if the events set forth above had been completed at the date indicated. In addition, the unaudited pro forma condensed combined statement of operations does not purport to project the future financial position or operating results of PAETEC.

The unaudited pro forma condensed combined statement of operations for the year ended December 31, 2010 combines the historical consolidated statements of operations for PAETEC and Cavalier to give effect to PAETEC s acquisition of Cavalier, PAETEC s $300 million senior secured notes offering completed on January 12, 2010, and PAETEC s $450 million senior notes offering completed on December 2, 2010 and the application of the proceeds therefrom, together with PAETEC and Cavalier cash on hand, to pay the merger consideration and other costs and expenses related to PAETEC s acquisition of Cavalier, including repayment of substantially all outstanding Cavalier indebtedness, as if they had occurred on January 1, 2010.

Issuance and Sale of 8 ^{7}/8% Senior Secured Notes. On January 12, 2010, PAETEC issued and sold $300 million in aggregate principal amount of 8 ^{7}/8% senior secured notes due 2017. PAETEC sold the senior secured notes at an offering price of 100.528% of their principal amount, plus accrued interest from December 31, 2009, and applied a portion of the proceeds of the offering to repay $240.2 million principal amount of term loans and $30.0 million principal amount of revolving loans outstanding under its senior secured credit facilities and to pay related fees and expenses. The $300 million of senior secured notes accrue interest at a rate of 8 ^{7}/8% per year. Interest is payable semi-annually in cash in arrears on June 30 and December 31 of each year. The 8 ^{7}/8% senior secured notes will mature on June 30, 2017.

The January 12, 2010 offering of PAETEC s 8^7/8% senior secured notes and the use of the proceeds of such offering was accounted for under the guidance in Accounting Standards Codification, or ASC, Topic 470,

30

Table of Contents

Debt, as an extinguishment. The historical condensed consolidated statement of operations for the year ended December 31, 2010 reflects $4.4 million of debt extinguishment and related costs recognized by PAETEC in connection with the January 12, 2010 issuance and sale of the $300 million of 8 $^7/_8$% senior secured notes and related repayment of loans outstanding under its senior secured credit facilities.

Issuance and Sale of 9 $^7/_8$% Senior Notes and Acquisition of Cavalier. On December 2, 2010, PAETEC Escrow Corporation, or PAETEC Escrow, a wholly-owned subsidiary of PAETEC Holding Corp., issued and sold $450 million in aggregate principal amount of its 9 $^7/_8$% senior notes due 2018. On December 2, 2010, the gross proceeds of approximately $435 million received from the offering of the 9 $^7/_8$% senior notes were deposited into a segregated escrow account.

On December 6, 2010, PAETEC Holding completed its acquisition of Cavalier by merger. Upon the effectiveness of the merger and the satisfaction of other conditions, PAETEC Holding assumed PAETEC Escrow s obligations and agreements in respect of the 9 $^7/_8$% senior notes and under the indenture governing such notes, and the escrow arrangements were terminated and the proceeds of the offering of the 9 $^7/_8$% senior notes were disbursed from the escrow account and used, together with cash on hand of PAETEC Holding and Cavalier, to pay the consideration and other costs and expenses related to the merger.

PAETEC s acquisition of Cavalier by merger on December 6, 2010 was accounted for using the acquisition method in accordance with ASC Topic 805, *Business Combinations*, or ASC 805. The purchase price allocation for the Cavalier merger is reflected in the historical consolidated balance sheet of PAETEC as of December 31, 2010, as included in PAETEC s Annual Report or Form 10-K for the year ended December 31, 2010. In accordance with ASC 805, the purchase price of the Cavalier merger was allocated to the assets acquired and liabilities assumed based on their fair values as of the merger closing date, with the amounts exceeding the fair value of the assets acquired being recorded as goodwill.

The unaudited pro forma condensed combined statement of operations for the year ended December 31, 2010 has been adjusted for the decreased depreciation expense resulting from the acquired property and equipment, as well as the increased amortization expense resulting from the acquired intangible assets.

This unaudited pro forma financial information is based on PAETEC management s estimates of fair values of acquired property and equipment and intangible assets. Definitive allocations will be finalized based upon valuations and other studies that were performed following the closing date of the merger. Accordingly, the depreciation and amortization adjustments are preliminary and have been made solely for the purpose of providing unaudited pro forma condensed combined financial information and are subject to revision based on a final determination of fair value. Final determinations of fair value may differ materially from those presented. The unaudited pro forma condensed combined statement of operations also includes certain purchase accounting adjustments, including items expected to have a continuing impact on the combined results, such as interest expense on PAETEC s $450 million offering of the 9 $^7/_8$% senior notes completed on December 2, 2010.

The unaudited pro forma condensed combined statement of operations does not include the effects of any revenue, cost or other operating efficiencies that may result from the Cavalier merger, nor does it reflect any other changes that might occur regarding the PAETEC and Cavalier combined portfolios of businesses.

The unaudited pro forma condensed consolidated statement of operations does not reflect any nonrecurring charges expected to result from the Cavalier merger, other than those actually realized and reflected in the historical consolidated statements of operations for PAETEC. The majority of nonrecurring charges resulting from the merger include employee termination, exit costs and other integration-related costs, as well as transaction costs such as investment banker, advisory, legal, and other professional fees.

Table of Contents

Unaudited Pro Forma Condensed Consolidated Statement of Operations

For the Year Ended December 31, 2010

(in thousands, except share and per share data)

	PAETEC Holding Historical[(a)]	8 7/8% Senior Secured Notes Pro Forma Adjustments	Subtotal	Cavalier Historical[(b)]	Cavalier Merger Pro Forma Adjustments and Pro Forma Adjustments for 9 7/8% Senior Notes	Pro Forma as Adjusted
Revenue	$ 1,623,816	$	$ 1,623,816	$ 354,959	$ (12,962)(f)	$ 1,965,813
Cost of sales (exclusive of operating items shown separately below)	808,892		808,892	159,673	(12,962)(f)	955,603
Selling, general and administrative expenses (exclusive of operating items shown separately below and inclusive of stock-based compensation)	559,673		559,673	112,901		672,574
Acquisition, integration and separation costs	14,124		14,124	12,683	(20,164)(g)	6,643
Depreciation and amortization	196,543		196,543	46,421	20,294(h)	263,258
Income from operations	44,584		44,584	23,281	(130)	67,735
Debt extinguishment and related costs	7,382	(4,423)[(c)]	2,959			2,959
Other income, net	(392)		(392)	(74)		(466)
Interest expense	96,339	635[(d)]	96,974	39,874	4,172(i)	141,020
(Loss) income from continuing operations before income taxes	(58,745)	3,788	(54,957)	(16,519)	(4,302)	(75,778)
(Benefit from) provision for income taxes	(1,004)	[(e)]	(1,004)	319	(319)(j)	(1,004)
Loss from continuing operations	$ (57,741)	$ 3,788	$ (53,953)	$ (16,838)	$ (3,983)	$ (74,774)
Loss per common share from continuing operations basic and diluted	$ (0.40)		$ (0.37)			$ (0.51)
Basic and diluted weighted average common shares outstanding	145,345,301		145,345,301			145,345,301

Table of Contents

Notes to Unaudited Pro Forma Condensed Combined Statement of Operations for the Year Ended December 31, 2010

(a) Includes results of Cavalier as of the Cavalier merger closing date of December 6, 2010.

(b) Represents results from January 1, 2010 through the Cavalier merger closing date of December 6, 2010.

(c) The decrease in debt extinguishment and related costs of $4.4 million represents the elimination of historical PAETEC costs recognized in connection with the January 12, 2010 issuance and sale of $300 million in aggregate principal amount of 8 7/8% senior secured notes and related repayment of loans outstanding under PAETEC s senior secured credit facilities. These historical costs are directly attributable to the issuance and sale of the 8 7/8% senior secured notes, and are not expected to have a continuing impact.

(d) The increase in interest expense of $0.6 million represents the following:

an increase of $0.9 million related to the interest expense on the 8 7/8% senior secured notes; and

a decrease of $0.3 million related to the elimination of historical PAETEC interest expense on PAETEC s indebtedness repaid with the proceeds of the offering of the 8 7/8% senior secured notes in January 2010.

(e) During the year ended December 31, 2010, PAETEC maintained a full valuation allowance for deferred tax assets. Accordingly, no pro forma adjustments to the provision for income taxes were recorded related to the adjustments in expenses described in notes (c) and (d) above.

(f) The decreases in both revenue and in cost of sales of $13.0 million represent the following:

a decrease of approximately $5.1 million in both revenue and in cost of sales to eliminate the impact of intercompany transactions between PAETEC and Cavalier for the period; and

a decrease of approximately $7.9 million in both revenue and in cost of sales to conform the historical results of Cavalier to the historical results of PAETEC with respect to the presentation of Universal Service Fund, or USF, taxes. Cavalier historically reported taxes collected from customers for the USF on a gross basis as revenue, and included the amounts remitted to the tax authorities for the USF in cost of sales. PAETEC presents USF taxes on a net basis.

(g) The decrease in acquisition, integration and separation costs of $20.2 million represents the following:

a decrease of approximately $8.0 million due to the elimination of historical PAETEC transaction costs directly related to the acquisition of Cavalier by PAETEC; and

a decrease of approximately $12.2 million due to the elimination of historical Cavalier transaction costs directly related to the acquisition of Cavalier by PAETEC.

(h) The increase in depreciation and amortization expense of $20.3 million represents the following:

an increase in amortization expense of approximately $20.8 million for the year ended December 31, 2010 based on an acquired fair value of Cavalier s intangible assets of $160.2 million with estimated useful lives of approximately 1-14 years, and utilizing an accelerated amortization method; and a decrease in depreciation expense of approximately $0.5 million for the year ended December 31, 2010 based on an acquired fair value of Cavalier s depreciable property and equipment of $229.0 million with a weighted average expected useful life of approximately 6.7 years.

Table of Contents

As the fair values assigned to the property and equipment and intangible assets acquired from Cavalier are preliminary in nature, actual depreciation and amortization expense in future periods may differ materially from the depreciation and amortization expense presented.

A change of $10 million in the fair value of the intangible assets acquired from Cavalier presented would result in a fluctuation of approximately $1.6 million in amortization expense during the year ended December 31, 2010.

A change of $10 million in the fair value of the property and equipment acquired from Cavalier presented would result in a fluctuation of approximately $1.5 million in depreciation expense during the year ended December 31, 2010.

(i) The increase in interest expense of $4.2 million represents the following:

- an increase of $43.8 million (of which $1.7 million represents amortization of debt discount and $1.3 million represents amortization of debt issue costs) related to the interest expense on the $450 million in aggregate principal amount of 9 $^{7}/8$% senior notes completed on December 2, 2010; and

- a decrease of $39.6 million (of which $2.2 million represents amortization of debt issue costs) related to the elimination of substantially all historical Cavalier interest expense on Cavalier s pre-merger indebtedness.

Pro forma interest expense was calculated based on the stated interest rate of the 9 $^{7}/8$% senior notes due 2018.

(j) During the year ended December 31, 2010, PAETEC maintained a full valuation allowance for deferred tax assets. Accordingly, Cavalier s historical benefit from income taxes was eliminated on a pro forma basis. In addition, no pro forma adjustments to the provision of income taxes were recorded related to Cavalier s historical net loss from continuing operations or the adjustments in expenses described in notes (f), (g), (h) and (i) above.

34

Table of Contents

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following management s discussion and analysis together with the consolidated financial statements and related notes and the other financial information that appear elsewhere in this prospectus.

Overview

PAETEC is a competitive broadband communications services and solutions provider guided by the principle that delivering superior customer service is the key to competing successfully with other communications services providers. PAETEC s primary business is providing business end-user customers in metropolitan areas with a package of integrated broadband services that encompasses data services, including Internet access services and virtual private network services, and voice services, including local telephone services and domestic and international long distance services. As of March 31, 2011, PAETEC provided services for over 54,000 business customers in a service area encompassing 86 of the top 100 metropolitan statistical areas.

Business Acquisitions

PAETEC pursues an acquisition strategy to supplement its internal growth. Pursuant to this strategy and as discussed elsewhere in this prospectus, on December 6, 2010, PAETEC completed its acquisition by merger of Cavalier Telephone Corporation, which became a wholly-owned subsidiary of PAETEC Holding upon completion of the merger. Cavalier is a facilities-based competitive communications services provider that delivers traditional circuit-switched telephony services and Internet Protocol-based communications services to customers in 16 states in the Mid-Atlantic, Southeast and Midwest regions of the United States, as well as in the District of Columbia. Cavalier provides commercial, consumer and government customers and other communications providers with high-quality voice and data communications services that include high-speed and dial-up Internet services, local and long distance telephone services, and transport services. Cavalier maintains one of the most extensive competitive networks in the Eastern United States, with approximately 16,600 route miles of fiber.

On February 8, 2011, PAETEC Holding entered into a merger agreement, by and among PAETEC Holding, XETA Technologies, Inc., which we refer to as XETA, and an indirect, wholly-owned subsidiary of PAETEC Holding, pursuant to which XETA will become a wholly-owned subsidiary of PAETEC Holding at the effective time of the merger. Under the merger agreement, XETA s security holders have the right to receive total merger consideration of approximately $61 million. The merger agreement has been approved unanimously by the board of directors of each of PAETEC Holding and XETA. The consummation of the merger is subject to customary conditions.

Indebtedness

To fund its expansion through acquisitions, which began in February 2007 with the combination of PAETEC Corp. and US LEC and included the acquisition of McLeodUSA in February 2008 and Cavalier in December 2010, PAETEC has increased its borrowings under a variety of debt arrangements. In connection with its acquisition of US LEC in 2007, PAETEC obtained $850 million aggregate principal amount of new senior secured credit facilities on February 28, 2007 and applied the proceeds of the facilities primarily to refinance or retire substantially all of the indebtedness of the two companies and to repurchase US LEC s outstanding preferred stock. In July 2007, PAETEC amended its senior secured credit facilities and prepaid $300 million aggregate principal amount of borrowings under those facilities with the proceeds of an offering of $300 million aggregate principal amount of its 9.5% senior notes and cash on hand. In January 2008, PAETEC obtained $100 million principal amount of additional term loans under an incremental facility extended pursuant to its existing

35

[Table of Contents](#)

credit facilities agreement and applied a portion of the borrowings under that facility toward the redemption of all of McLeodUSA s outstanding senior secured notes in connection with PAETEC s acquisition of McLeodUSA.

In June 2009, to strengthen its financial position, PAETEC prepaid $330.5 aggregate million principal amount of borrowings under its senior secured credit facilities with the proceeds of an offering of $350 million aggregate principal amount of PAETEC Holding s 8 7/8% senior secured notes and cash on hand. In January 2010, PAETEC prepaid the remaining $270.2 million principal amount of borrowings under its senior secured credit facilities with the proceeds of an offering of $300 million aggregate principal amount of additional 8 7/8% senior secured notes. As a result of the two offerings, PAETEC eliminated its outstanding borrowings under its senior secured credit facilities and extended its debt maturities to 2015 and 2017 with limited impact to its cash flow generation capabilities.

In December 2010, PAETEC issued $450 million aggregate principal amount of the 9 7/8% senior notes subject to the exchange offer covered by this prospectus and applied the proceeds to pay the merger consideration and other costs and expenses related to PAETEC s acquisition of Cavalier, including repayment of substantially all outstanding Cavalier indebtedness.

Trends Affecting Our Business

General Economic Slowdown. Adverse conditions in the global economy in recent years have reduced the availability of corporate credit, negatively affected employment levels and curtailed corporate growth and expansion. These conditions and other factors have contributed to a slowdown of business activity across a broad range of industries. PAETEC believes that the financial and economic pressures faced by its business customers in this environment of diminished consumer spending, corporate downsizing and tightened credit have had, and may continue to have, an adverse effect on billable minutes of use and on customer attrition rates, and have resulted in and may continue to result in increased customer demands for price reductions in connection with contract renewals. In addition, as a result of the current conditions, PAETEC s ability to access further the debt and equity markets may be restricted at a time when it would like, or need, to access such markets, which could have an adverse effect on PAETEC s flexibility to react to changing economic and business conditions. The disruptions in the financial markets have had, and may continue to have, an adverse effect on the market value of PAETEC s common stock, which could make it more difficult or costly for the company to raise capital through an offering of its equity securities.

Shifting Patterns of Use and Convergence of Technology. As telecommunications customers increasingly use wireless forms of communication, such as hand-held Internet access devices and cell phones, the volume of traffic carried by traditional wireline telecommunications networks has declined and is expected to continue to decline. Although PAETEC believes this trend is most pronounced in the residential marketplace, wireless substitution also has had an adverse effect on the wireline usage patterns of the medium-sized and large businesses and institutions PAETEC targets. PAETEC believes that wireless substitution has led to a decrease in the average minutes of use generated by its customers. To date, PAETEC has been able partially to offset this loss of revenue from existing customers through sales of services to new customers. PAETEC believes that the transition to wireless-based forms of communication will continue in the foreseeable future. PAETEC seeks to respond to this trend by offering service levels and product packages that are not currently available using wireless alternatives.

Voice and data traffic historically have traveled over telecommunications networks using incompatible transmission formats. This means that a telecommunications transmission circuit had to be designated to carry either data traffic or voice traffic. As a result, excess capacity on a voice circuit could not be made available to reduce demand on a data circuit. VoIP technology, which allows voice and data traffic to travel interchangeably over the same network, enables more efficient use of the telecommunications networks. Because PAETEC leases the majority of its transmission capacity, the increased efficiency has the potential to reduce significantly PAETEC s cost of providing services to its customers. PAETEC continues to install equipment and transition its

Table of Contents

network to take advantage of these new technologies. PAETEC believes that, in operating a network using both traditional voice and newer VoIP technology, it is one of the leading competitive carriers in pursuing the benefits of technological convergence.

As PAETEC s customers migrate their traditional voice services to VoIP technology, PAETEC is experiencing a decline in usage-based revenues. In addition, the combination of shifting patterns of use and increasing convergence of voice and data traffic could make it harder for PAETEC to sustain and improve its operating margins over the next several years. PAETEC believes that the challenges these trends may present will be offset in part by the efficiencies of operating a data network to which it will increasingly transition its traditional voice services.

Competition; Evolving Regulatory Environment; Industry Consolidation. The telecommunications industry has remained highly competitive in an environment marked by increased deregulation. Market forces and changes in government regulations have required, and may continue to require, PAETEC to reduce rates for some of the services it provides. These trends may reduce PAETEC s historical rate of revenue growth and continue to exert pressure on its operating margins. PAETEC believes that the relatively long-term nature of its agreements with customers of its network services, which as of March 31, 2011 have an average initial term of 36 months, should reduce the likelihood that it will experience significant, rapid decreases in the rates it charges for its services.

Mergers involving the RBOCs and deregulatory activity favoring RBOCs at both federal and state levels over the past several years have made it more difficult to compete against these larger, financially stronger competitors. Additional regulatory changes that would permit incumbent carriers to materially increase rates charged for interconnecting networks and accessing last mile connections or to reduce PAETEC s rates for certain network services could make it more difficult for our company to remain competitive.

PAETEC s industry has experienced a significant amount of consolidation in recent periods. Merger and acquisition transactions have created more significant competitors for PAETEC and have reduced the number of vendors from which PAETEC may purchase network elements it leverages to operate its business. PAETEC expects this trend to continue in the near future. To compete more effectively in its industry, PAETEC plans to continue pursuing its historical acquisition strategy to increase its operating leverage, achieve economies of scale and broaden its name recognition.

Financial Difficulties Faced by Many Competitive Communications Carriers. Over the last decade, many competitive communications services providers have experienced financial difficulties. These difficulties have led to the general perception that the competitive carrier sector of PAETEC s industry is marred by instability and financial weakness. This perception makes it harder for PAETEC to gain new customers, raise additional capital and negotiate with vendors. PAETEC has addressed this perception by maintaining cash balances that are generally in excess of its current needs and by managing its growth activities so that its short-term cash flow is not impaired.

Revenue

PAETEC derives revenue from sales of its network services, carrier services and integrated solutions services. PAETEC derives most of its revenue from monthly recurring fees and usage-based fees that are generated principally by sales of its network services.

Monthly recurring fees include the fees paid by PAETEC s customers for lines in service and additional features on those lines. PAETEC primarily bills monthly recurring fees in advance.

Usage-based fees consist of fees paid by PAETEC s network services customers for each call made, fees paid by the incumbent carriers in PAETEC s markets as reciprocal compensation when PAETEC terminates local calls made by their customers, and access fees paid by other carriers for long distance calls PAETEC originates or terminates for those carriers.

Table of Contents

The monthly recurring fees and usage-based fees generated by sales of PAETEC s network services to end users and carrier services to any customer tend to be relatively consistent from month to month, subject to changes in the calling patterns of the customer s business.

Network Services. PAETEC delivers integrated communications services, including data and Internet services, local services and long distance services, to end users on a retail basis, which the company refers to as its network services.

PAETEC s network services revenue consists primarily of monthly recurring fees and usage-based fees. In addition to usage-based fees invoiced directly to the end-user customers, usage-based fees for PAETEC s network services include the interstate and intrastate access fees the company receives from other communications providers when it originates or terminates long-distance calls for those other providers to or from PAETEC s network services customers, and the reciprocal compensation fees PAETEC receives from some other local carriers when it terminates non-toll calls originated by customers of other carriers. PAETEC recognizes revenue during the period in which the revenue is earned. PAETEC s network services also generate non-recurring service activation and installation fee revenues, which it receives upon initiation of service. PAETEC defers recognition of these revenues and amortizes them over the average customer life.

PAETEC s core network services are those that generate revenue from retail enterprise customers to which PAETEC delivers such integrated communications services on primarily T1 or larger access lines, which excludes access fee and reciprocal compensation fee revenue related to network services and revenue from the company s POTS operations. POTS operations involve the provision of basic telephone services supplying standard single line telephones, telephone lines and access to the public switched network.

Carrier Services. PAETEC generates revenue from wholesale sales of communications services to other communications businesses, which the company refers to as its carrier services.

PAETEC s carrier services revenue consists primarily of monthly recurring fees and usage-based fees. Usage-based fees for PAETEC s carrier services consist primarily of the interstate and intrastate access fees the company receives from other communications providers when it originates or terminates long distance calls for those other providers to or from PAETEC s carrier services customers, and the reciprocal compensation fees PAETEC receives from some other local carriers when it terminates to its carrier services customers local calls made by customers of other local carriers.

PAETEC s core carrier services are those that generate revenue from other communications providers, which excludes access fee and reciprocal compensation fee revenue related to carrier services and revenue from the company s non-core POTS operations.

Access Fee and Reciprocal Compensation Revenue Generated by Network Services and Carrier Services. PAETEC generates access fees when PAETEC s switching facilities provide a connection between a long distance carrier and an end user. In accordance with a May 2004 order by the FCC, PAETEC has designed its interstate access rates to equal the interstate access rates charged by the competing incumbent carrier for functionally equivalent access services, including all applicable fixed and traffic-sensitive charges. In the May 2004 order, the FCC announced a new rule that limits the interstate access fees competitive carriers like PAETEC are able to collect from a long distance carrier in situations where the competitive carriers do not provide service directly to the end user. This rule specifically targeted traffic that competitive carriers handle for wireless carriers and provided that competitive carriers could charge no more than incumbent carriers for these services.

State regulatory commissions historically have regulated the intrastate access rates imposed by incumbent carriers, but many states had subjected the intrastate access rates of competitive carriers to significantly less regulation. A limited number of states in PAETEC s geographic markets have always required competitive carriers to mirror the intrastate access rates of the incumbent carrier in that state or mirror interstate rate levels. In recent years, however, several states have implemented new laws or adopted new regulations that limit the intrastate access rates of competitive carriers. Massachusetts, Michigan, New Jersey and Illinois have

imposed limits on such intrastate access rates that require the rates to be reduced to match the level of RBOC rates over transition periods of varying lengths. Other state regulatory commissions have pending investigations into intrastate access rates of competitive carriers, while legislation has been proposed in some states to impose similar rate caps. Those proceedings and legislative proposals may result in changes to the intrastate rates, which PAETEC assesses long distance carriers for use of the PAETEC s in-state networks.

All forms of intercarrier compensation, including exchange access and reciprocal compensation, currently are the subject of a generic proceeding at the FCC designed to reform the way carriers and providers pay other carriers and providers for use of their respective networks.

Integrated Solutions. PAETEC derives revenue from sales to retail end-user customers of telecommunications equipment and software and related services and energy supply services, which the company refers to collectively as its integrated solutions.

A portion of PAETEC s integrated solutions revenue consists of fees its customers pay for equipment and for PAETEC s system design and installation services. PAETEC recognizes revenue for equipment sales and system design and installation services upon delivery and acceptance of the underlying installed equipment.

PAETEC derives an additional component of its integrated solutions revenue by selling and supporting its proprietary telecommunications software. PAETEC recognizes revenue related to software sales upon delivery of the software. Support fees include fees for maintenance of PAETEC s telecommunications software and fees for training the end user in the proper use of that software. PAETEC recognizes maintenance fees on a pro rata basis over the length of the underlying maintenance contract and training fees after it fulfills the training obligation.

Energy supply services revenue consists primarily of usage-based fees its customers pay for unregulated electricity. Revenues are subject to variability based upon market factors. PAETEC recognizes revenue related to energy sales when the service is provided.

Cost of Sales

PAETEC provides its network services and carrier services by using electronic network components that it owns and telephone and data transmission lines that it leases from other telecommunications carriers. PAETEC s cost of sales for these services consists primarily of leased transport charges and usage costs for local and long distance calls. PAETEC s leased transport charges are the payments it makes to lease the telephone and data transmission lines, which the company uses to connect its customers to its network and to connect its network to the networks of other carriers. Usage costs for local and long distance are the costs that PAETEC incurs for calls made by its customers. Cost of sales for PAETEC s integrated solutions includes the costs it incurs in designing systems and purchasing and installing equipment and the costs incurred in procuring electricity from the market operators on a wholesale basis.

Selling, General and Administrative Expenses

PAETEC s selling, general and administrative expenses include selling and marketing, customer service, billing, corporate administration, engineering personnel and other personnel costs.

Impairment Charge

PAETEC assesses the carrying value of its goodwill annually or as events or circumstances change. In accordance with its impairment assessment process, PAETEC recorded a non-cash impairment charge of $340.0

Table of Contents

million in the third quarter of 2008 based on a preliminary assessment in that quarter, and recorded an additional non-cash charge of $15.0 million in the fourth quarter of 2008 based on the finalization of that preliminary assessment. The goodwill impairment charges were attributable to weaker economic conditions in PAETEC s markets. For more information about PAETEC s impairment review policies, see Critical Accounting Policies below. For information about PAETEC s goodwill, see Note 5 to PAETEC s audited consolidated financial statements appearing elsewhere in this prospectus.

Depreciation and Amortization

Depreciation and amortization include depreciation of PAETEC s telecommunications network and equipment, computer hardware and purchased software, office equipment, furniture and fixtures, and buildings, as well as amortization of intangible assets.

Acquisition, Integration and Separation Costs

Acquisition, integration and separation costs include external costs directly related to PAETEC s acquisition activities, such as advisory, legal, accounting, valuation and other professional fees. In addition, such costs include employee severance and benefit costs associated with PAETEC s acquisition activities.

Debt Extinguishment and Related Costs

PAETEC s debt extinguishment and related costs include expenses related to the repayment of outstanding term loans under PAETEC s senior secured credit facilities, costs incurred related to PAETEC s former interest rate swap agreement and expenses related to the termination of a financing commitment. For information about PAETEC s debt transactions, see Note 6 to PAETEC s audited consolidated financial statements appearing elsewhere in this prospectus.

Interest Expense

Interest expense includes interest due on PAETEC s long-term debt and capital leases, amortization of debt issuance costs, debt premiums, and debt discounts.

Other Income, Net

Other income, net includes investment income, non-monetary gains on the exchange of reciprocal indefeasible rights of use, or IRUs, and other financing income.

Accounting for Income Taxes

PAETEC recognizes deferred income tax assets and liabilities for the expected future tax consequences of transactions and events. Under this method, PAETEC determines deferred income tax assets and liabilities based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which it expects the differences to reverse. If necessary, PAETEC reduces deferred income tax assets by a valuation allowance to an amount that it determines is more likely than not to be recoverable.

Stock-Based Compensation

PAETEC s employees participate in a variety of equity incentive plans. Stock-based compensation expense for all stock-based compensation awards is based on the grant date fair value estimated in accordance with the Financial Accounting Standards Board, or FASB, Accounting Standard Codification, or ASC, Topic 718, *Compensation Stock Compensation*. PAETEC recognizes these compensation costs, net of an estimated forfeiture rate, ratably over the requisite service period of the award.

Table of Contents

Adjusted EBITDA Presentation

Adjusted EBITDA, as defined by PAETEC for the periods presented in this management s discussion and analysis, represents net (loss) income before depreciation and amortization, interest expense, provision for (benefit from) income taxes, stock-based compensation, acquisition, integration and separation costs, debt extinguishment and related costs, sales and use tax settlement, gain on non-monetary transaction and impairment charges. PAETEC s adjusted EBITDA is not a measure of financial performance under GAAP. This non-GAAP financial measure is used by PAETEC s management, together with financial measurements prepared in accordance with GAAP such as net (loss) income and revenue, to assess PAETEC s historical and prospective operating performance.

Management uses adjusted EBITDA to enhance its understanding of PAETEC s core operating performance, which represents management s views concerning PAETEC s performance in the ordinary, ongoing and customary course of its operations. Management historically has found it helpful, and believes that investors have found it helpful, to consider an operating measure that excludes expenses, such as acquisition, integration and separation costs, debt extinguishment and related costs, and impairment charges, relating to transactions not reflective of PAETEC s core operations. In the future, the company expects that it may again report adjusted EBITDA excluding the items discussed below and may incur expenses similar to the excluded items discussed below. Accordingly, the exclusion of these and other similar items in PAETEC s non-GAAP presentation should not be interpreted as implying that these items are non-recurring, infrequent or unusual. Management believes that, for the reasons discussed below, PAETEC s use of a supplemental financial measure which excludes these expenses facilitates an assessment of PAETEC s fundamental operating trends and addresses concerns of management and of PAETEC s investors that these expenses may obscure such underlying trends. Management notes that each of these expenses is presented in PAETEC s financial statements and discussed in the management s discussion and analysis section of PAETEC s reports filed with the Securities and Exchange Commission, so that investors have complete information about the expenses.

The information about PAETEC s core operating performance provided by this financial measure is used by management for a variety of purposes. Management regularly communicates its adjusted EBITDA results to its board of directors and discusses with the board management s interpretation of such results. Management also compares the company s adjusted EBITDA performance against internal targets as a key factor in determining cash bonus compensation for executives and other employees, largely because management feels that this measure is indicative of the how the fundamental business is performing and is being managed. In addition, PAETEC s management uses adjusted EBITDA to evaluate PAETEC s performance relative to that of its competitors. This financial measure permits a comparative assessment of PAETEC s operating performance relative to the company s performance based on its GAAP results, while isolating the effects of certain items that vary from period to period without any correlation to core operating performance or that vary widely among similar companies.

Management believes that adjusted EBITDA is a particularly useful comparative measure within PAETEC s industry. The communications industry has experienced recent trends of increased merger and acquisition activity and financial restructurings. These activities have led to significant charges to earnings, such as those resulting from acquisition, integration and debt restructuring costs, and to significant variations among companies with respect to capital structures and cost of capital (which affect interest expense) and differences in taxation and book depreciation of facilities and equipment (which affect relative depreciation expense),

including significant differences in the depreciable lives of similar assets among various companies. Adjusted EBITDA facilitates company-to-company comparisons in the communications industry by eliminating some of the foregoing variations. Management believes that because of the variety of equity awards used by companies, the varying methodologies for determining both stock-based compensation and stock-based compensation expense among companies and from period to period, and the subjective assumptions involved in those determinations, excluding stock-based compensation from adjusted EBITDA enhances company-to-company comparisons over multiple fiscal periods. By permitting investors to review both the GAAP and non-GAAP measures, PAETEC and its peers that customarily use similar non-GAAP measures facilitate an enhanced understanding of historical financial results and enable investors to make more meaningful company-to-company comparisons.

PAETEC also provides information relating to its adjusted EBITDA so that analysts, investors and other interested persons have the same data that management uses to assess PAETEC s core operating performance. Management believes that adjusted EBITDA should be viewed only as a supplement to the GAAP financial information. Management also believes, however, that providing this information in addition to, and together with, GAAP financial information permits the foregoing persons to obtain a better understanding of PAETEC s core operating performance and to evaluate the efficacy of the methodology and information used by management to evaluate and measure such performance on a standalone and a comparative basis.

PAETEC s adjusted EBITDA may not be directly comparable to similarly titled measures reported by other companies due to differences in accounting policies and items excluded or included in the adjustments, which limits its usefulness as a comparative measure. In addition, adjusted EBITDA has other limitations as an analytical financial measure. These limitations include the following:

- adjusted EBITDA does not reflect PAETEC s capital expenditures, future requirements for capital expenditures or contractual commitments to purchase capital equipment;
- adjusted EBITDA does not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, associated with PAETEC s indebtedness;
- although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will likely have to be replaced in the future, and adjusted EBITDA does not reflect any cash requirements for such replacements;
- adjusted EBITDA does not reflect the cost of equity awards to employees;
- adjusted EBITDA excludes some items in addition to stock-based compensation that are likely to recur;
- adjusted EBITDA does not reflect the effect of earnings or charges resulting from matters that PAETEC s management considers not indicative of PAETEC s ongoing operations; and
- to the extent that PAETEC changes its accounting of certain transactions or other items from period to period, PAETEC s adjusted EBITDA may not be directly comparable from period to period.

PAETEC s management compensates for these limitations by relying primarily on PAETEC s GAAP results to evaluate its operating performance and by considering independently the economic effects of the foregoing items that are or are not reflected in adjusted EBITDA. Management also compensates for these limitations by providing GAAP-based disclosures concerning the excluded items in its financial disclosures. As a result of these limitations, however, adjusted EBITDA should not be considered as an alternative to net (loss) income, as calculated in accordance with GAAP, as a measure of operating performance, or as an alternative to any other GAAP measure of operating performance.

Results of Operations

The following table presents selected operating data for the fiscal years ended December 31, 2010, 2009 and 2008 and for the three-month periods ended March 31, 2011 and 2010. In the following comparisons of PAETEC s operating results, we refer to the three months ended March 31, 2011 as our 2011 quarter and the three months ended March 31, 2010 as our 2010 quarter. The comparisons of PAETEC s operating results for 2011 to PAETEC s operating results for 2010 are materially affected by PAETEC s acquisition of Cavalier on December 6, 2010. Cavalier s operating results are included in PAETEC s operating results beginning on December 6, 2010. In addition, the following comparison of PAETEC s operating results for 2009 to PAETEC s operating results for 2008 is materially affected by PAETEC s acquisition of McLeodUSA on

February 8, 2008.

Table of Contents

McLeodUSA s operating results are included in PAETEC s operating results beginning on February 9, 2008. Because of the significance of each merger transaction, PAETEC s operating results for 2010, 2009 and 2008 are not directly comparable. PAETEC s operating results for those years were as follows (dollars in thousands):

	Year Ended December 31,						Three Months Ended March 31,			
	2010[1]		2009		2008[2]		2011		2010	
	$	% of Revenue	$	% of Revenue	$	% of Revenue	$	% of Revenue	$	% of Revenue
Revenue:										
Network services	$ 1,245,157	77%	$ 1,258,489	80%	$ 1,237,668	79%	$ 377,032	76%	$ 310,474	80%
Carrier Services	262,749	16%	260,023	16%	271,279	17%	82,212	17%	63,043	16%
Integrated solutions	115,910	7%	61,675	4%	61,433	4%	36,269	7%	16,534	4%
Total revenue	1,623,816	100%	1,580,187	100%	1,570,380	100%	495,513	100%	390,051	100%
Cost of sales[3]	808,892	50%	782,389	50%	781,347	50%	233,912	47%	192,749	49%
Selling, general and administrative expenses[4]	559,673	34%	559,541	35%	572,180	36%	172,692	35%	134,260	34%
Acquisition, integration and separation costs	14,124	1%		*	12,700	1%	2,493	*		*
Sales and use tax settlement		*	(7,221)	*		*		*		*
Impairment charge		*		*	355,000	23%		*		*
Depreciation and amortization	196,543	12%	184,588	12%	174,251	11%	63,313	13%	47,173	12%
Income (loss) from operations	44,584	3%	60,890	4%	(325,098)	(21%)	23,103	5%	15,869	4%
Debt extinguishment and related costs	7,382	*	17,891	1%		*		*	4,423	1%
Other income, net	(392)	*	(1,107)	*	(663)	*	(81)	*	(112)	*
Interest expense	96,339	6%	74,149	5%	73,663	5%	34,464	7%	22,037	6%
Loss before income taxes	(58,745)	(4)%	(30,043)	(2)%	(398,098)	(25)%	(11,280)	(2)%	(10,479)	(3)%
(Benefit from) provision for income taxes	(1,004)	*	(1,354)	*	89,797	6%	650	*	(941)	*
Net loss	$ (57,741)	(4)%	$ (28,689)	(2)%	$ (487,895)	(31)%	$ (11,930)	(2)%	$ (9,538)	(2)%
Adjusted EBITDA[5]	$ 264,931		$ 256,933		$ 237,725		$ 91,355		$ 65,543	

* Less than one percent.

(1) Includes the results of Cavalier as of the Cavalier merger closing date of December 6, 2010.

(2) Includes results of McLeodUSA after the McLeodUSA merger closing date of February 8, 2008.

(3) Exclusive of operating items shown separately below.

(4) Exclusive of operating items shown separately below and inclusive of stock-based compensation.

(5) Adjusted EBITDA is not a financial measurement prepared in accordance with GAAP. See Overview Adjusted EBITDA Presentation for PAETEC s reasons for including adjusted EBITDA data in this prospectus and for material limitations with respect to the usefulness of this measurement. The following table sets forth, for the periods indicated, a reconciliation of adjusted EBITDA to net loss, as net loss is calculated in accordance with GAAP (in thousands):

	Year Ended December 31,			Three Months Ended March 31,	
	2010	2009	2008	2011	2010
Net loss	$ (57,741)	$ (28,689)	$ (487,895)	$ (11,930)	$ (9,538)
Add back non-EBITDA items included in net loss:					

Depreciation and amortization	196,543	184,588	174,251	63,313	47,173
Interest expense, net of interest income	95,911	73,188	71,857	34,413	21,964
(Benefit from) provision for income taxes	(1,004)	(1,354)	89,797	650	(941)
EBITDA	233,709	227,733	(151,990)	86,446	58,658
Stock-based compensation	9,716	18,772	22,015	2,416	2,462
Acquisition, integration and separation costs	14,124		12,700	2,493	
Debt extinguishment and related costs	7,382	17,891			4,423
Sales and use tax settlement		(7,221)			
Gain on non-monetary transaction		(242)			
Impairment charge			355,000		
Adjusted EBITDA	$ 264,931	$ 256,933	$ 237,725	$ 91,355	$ 65,543

Table of Contents

Three Months Ended March 31, 2011 Compared With Three Months Ended March 31, 2010

Revenue. Total revenue increased $105.5 million, or 27.0%, to $495.5 million for the 2011 quarter from $390.1 million for the 2010 quarter primarily from the inclusion of operating results from Cavalier and other recently acquired businesses for the full 2011 quarter. Of total revenue for the 2011 quarter, revenue from network services, carrier services and integrated solutions accounted for 76.1%, 16.6% and 7.3%, respectively, compared to 79.6%, 16.2% and 4.2%, respectively, for the 2010 quarter.

Revenue from network services increased $66.6 million, or 21.4%, to $377.0 million for the 2011 quarter from $310.5 million for the 2010 quarter. Of total network services revenue for the 2011 quarter, revenue from core network services, access fee and reciprocal compensation revenue related to network services, and non-core POTS revenue related to network services accounted for 89.3%, 4.0% and 6.7%, respectively, compared to 91.2%, 5.7% and 3.1%, respectively, for the 2010 quarter.

Revenue from core network services increased $53.7 million, or 19.0%, to $336.8 million for the 2011 quarter from $283.1 million for the 2010 quarter. For the 2011 quarter, revenue from monthly recurring fees and usage-based fees accounted for 80.2% and 19.9%, respectively, of revenue from core network services, compared to 77.6% and 21.8%, respectively, of such revenue for the 2010 quarter. The increase in core network services revenue primarily resulted from the inclusion of Cavalier s operating results for the full 2011 quarter.

Access fee revenue and reciprocal compensation included in network services revenue decreased $2.9 million, or 16.2%, to $14.9 million for the 2011 quarter from $17.8 million for the 2010 quarter. Of total access fee revenue and reciprocal compensation included in network services for the 2011 quarter, revenue from access fees accounted for 92.1% compared to 91.8% for the 2010 quarter.

Non-core POTS revenue included in network services revenue increased $15.8 million, or 165%, to $25.3 million for the 2011 quarter from $9.5 million for the 2010 quarter. The increase in non-core POTS revenue primarily resulted from the inclusion of Cavalier s operating results for the full 2011 quarter, the effect of which was partially offset by customer attrition during the quarter.

Revenue from carrier services increased $19.2 million, or 30.4%, to $82.2 million for the 2011 quarter from $63.0 million for the 2010 quarter. Of total carrier services revenue for the 2011 quarter, revenue from core carrier services, access fee and reciprocal compensation revenue related to carrier services, and non-core POTS revenue related to carrier services accounted for 72.0%, 24.5% and 3.5%, respectively, compared to 70.8%, 23.4% and 5.8%, respectively, for the 2010 quarter.

Revenue from core carrier services increased $14.6 million, or 32.6%, to $59.2 million for the 2011 quarter from $44.7 million for the 2010 quarter. The increase in core carrier services revenue primarily resulted from the inclusion of Cavalier s operating results for the full 2011 quarter. For the 2011 quarter, revenue from monthly recurring fees and usage-based fees accounted for 67.6% and 20.0%, respectively, of revenue from core carrier services, compared to 59.9% and 27.1%, respectively, of such revenue for the 2010 quarter.

Access fee revenue and reciprocal compensation included in carrier services revenue increased $5.4 million, or 36.4%, to $20.1 million for the 2011 quarter from $14.7 million for the 2010 quarter. Of total access fee revenue and reciprocal compensation included in carrier services revenue for the 2011 quarter, revenue from access fees accounted for 88.8% compared to 83.0% for the 2010 quarter.

Non-core POTS revenue included in carrier services revenue decreased $0.8 million, or 21.3%, to $2.9 million for the 2011 quarter from $3.6 million for the 2010 quarter. The decrease in non-core POTS revenue primarily resulted from customer attrition.

Revenue from integrated solutions services increased $19.8 million, or 119.4%, to $36.3 million for the 2011 quarter from $16.5 million for the 2010 quarter. The increase in integrated solution services revenue

Table of Contents

primarily resulted from growth in both equipment sales and energy supply services due to the inclusion of operating results from U.S. Energy Partners LLC and Quagga Corporation for the full 2011 quarter.

Cost of Sales. Cost of sales increased to $233.9 million for the 2011 quarter from $192.7 million for the 2010 quarter, in part because of increased costs associated with the acquisition of Cavalier, increased costs associated with equipment sales due to the June 2010 acquisition of Quagga Corporation, and costs incurred to procure electricity from market operators on a wholesale basis.

Leased transport charges increased to $177.2 million, or 75.8% of cost of sales, for the 2011 quarter from $153.0 million, or 79.3% of cost of sales, for the 2010 quarter.

Usage costs for local and long distance calls increased to $33.4 million, or 14.3% of cost of sales, for the 2011 quarter from $29.5 million, or 15.3% of cost of sales, for the 2010 quarter.

Cost of sales as a percentage of total revenue decreased to 47.2% for the 2011 quarter from 49.4% for the 2010 quarter. The improvement was driven by a broad array of operational enhancements, including the contribution of higher margin Cavalier revenues, improved local network cost resulting from earlier initiatives to transition special access circuits to unbundled network elements, and an increase in integrated equipment and network sales driven by our IP Simple Product, which leverages PAETEC s proprietary Allworx platform.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased to $172.7 million for the 2011 quarter from $134.3 million for the 2010 quarter primarily due to costs associated with higher staffing levels in PAETEC s sales force and additional growth in headcount from acquisitions completed during 2010. Selling, general and administrative expenses as a percentage of total revenue increased to 34.9% for the 2011 quarter from 34.4% for the 2010 quarter.

Acquisition, Integration and Separation Costs. During the 2011 quarter, PAETEC recognized approximately $2.5 million of acquisition, integration and separation costs. These costs were primarily related to employee separations.

Depreciation and Amortization. Depreciation and amortization expense increased to $63.3 million for the 2011 quarter from $47.2 million for the 2010 quarter. The increase was primarily attributable to the inclusion of Cavalier s operating results for the full 2011 quarter and PAETEC s network deployment and maintenance activities.

Debt Extinguishment and Related Costs. During the 2010 quarter, PAETEC recognized a total of $4.4 million of debt extinguishment and related costs, which represented the elimination of $3.6 million of debt issuance costs and unamortized debt discount associated with the repayment of $240.2 million aggregate principal amount of term loans and $30.0 million aggregate principal amount of revolving loans outstanding under its senior secured credit facilities with the proceeds from the January 2010 issuance of $300.0 million aggregate principal amount of its 8 $^{7}/8$% senior secured notes and $0.8 million of costs related to the termination of its interest rate swap agreement.

Interest Expense. PAETEC s average outstanding debt balances increased to $1,470.2 million for the 2011 quarter from $946.0 million for the 2010 quarter, as a result of the December 2010 issuance of $450.0 million aggregate principal amount of the 9 $^{7}/8$% senior notes subject to the exchange offer covered by this prospectus. Interest expense increased to $34.5 million for the 2011 quarter from $22.0 million for the 2010 quarter due primarily to an increase in the average outstanding debt balances and an increase in the average annual borrowing rate. The weighted average annual borrowing rate, including the amortization of the debt discount and the debt premium but excluding the amortization of deferred financing costs, for the 2011 quarter was 9.4%, compared to 9.1% for the 2010 quarter.

Table of Contents

Income Taxes. The provision for income taxes for the 2011 quarter was $0.7 million. The difference between the statutory rate and the effective tax rate for the 2011 quarter was primarily attributable to the existence of a valuation allowance on PAETEC s net deferred tax assets.

2010 Compared With 2009

Revenue. Total revenue increased $43.6 million, or 2.8%, to $1,623.8 million for 2010 from $1,580.2 million for 2009, primarily because of revenue attributable to acquisitions during 2010, the effect of which was substantially offset by declines in usage-based revenue and non-core POTS revenue. Of total revenue for 2010, revenue from network services, carrier services and integrated solutions accounted for 76.7%, 16.2% and 7.1%, respectively, compared to 79.6%, 16.5% and 3.9%, respectively, for 2009.

Revenue from network services decreased $13.3 million, or 1.1%, to $1,245.2 million for 2010 from $1,258.5 million for 2009. Of total network services revenue for 2010, revenue from core network services, access fee and reciprocal compensation fee revenue related to network services, and non-core POTS revenue related to network services accounted for 91.6%, 5.2% and 3.2%, respectively, compared to 90.7%, 5.7% and 3.6%, respectively, for 2009.

Revenue from core network services decreased $1.3 million, or 0.1%, to $1,140.5 million for 2010 from $1,141.8 million for 2009. For 2010, revenue from monthly recurring fees and usage-based fees accounted for 78.1% and 21.6%, respectively, of revenue from core network services, compared to 76.7% and 22.5%, respectively, of such revenue for 2009. The decrease in core network services revenue primarily resulted from a decline in usage-based revenue and compression associated with the migration of traditional voice customers to newer VoIP technology. The revenue impact of these factors was partially offset by an increase in data revenue generated by increased sales of Dynamic IP and MPLS VPN products and the inclusion of Cavalier s results.

Access fee revenue and reciprocal compensation included in network services revenue decreased $6.1 million, or 8.6%, to $65.4 million for 2010 from $71.5 million for 2009. Of total access fee revenue and reciprocal compensation included in network services for 2010, revenue from access fees accounted for 91.6% compared to 90.2% for 2009.

Non-core POTS revenue included in network services revenue decreased $5.8 million, or 12.9%, to $39.3 million for 2010 from $45.1 million for 2009. The decrease in non-core POTS revenue primarily resulted from continued customer attrition.

Revenue from carrier services increased $2.7 million, or 1.0%, to $262.7 million for 2010 from $260.0 million for 2009. Of total carrier services revenue for 2010, revenue from core carrier services, access fee and reciprocal compensation fee revenue related to carrier services, and non-core POTS revenue related to carrier services accounted for 70.4%, 24.6% and 5.0%, respectively, compared to72.1%, 21.1% and 6.8%, respectively, for 2009.

Revenue from core carrier services decreased $2.5 million, or 1.3%, to $184.9 million for 2010 from $187.4 million for 2009. The decrease in core carrier services revenue primarily resulted from a decline in usage-based revenue. For 2010, revenue from monthly recurring fees and usage-based fees accounted for 59.8% and 26.8%, respectively, of revenue from core carrier services, compared to 56.1% and 30.9%, respectively, of such revenue for 2009.

Access fee revenue and reciprocal compensation included in carrier services revenue increased $9.6 million, or 17.5%, to $64.5 million for 2010 from $54.9 million for 2009. Of total access fee revenue and reciprocal compensation included in carrier services revenue for 2010, revenue from access fees accounted for 85.8% compared to 77.0% for 2009.

Table of Contents

Non-core POTS revenue included in carrier services revenue decreased $4.4 million, or 24.7%, to $13.3 million for 2010 from $17.7 million for 2009. The decrease in non-core POTS revenue primarily resulted from continued customer attrition.

Revenue from integrated solutions services increased $54.2 million, or 87.9%, to $115.9 million for 2010 from $61.7 million for 2009. Of this increase, $44.6 million was attributable to growth in both equipment sales and energy services as a result of business acquisitions during 2010.

Cost of Sales. Cost of sales increased to $808.9 million for 2010 from $782.4 million for 2009, in part because of an increase in special access rates and associated unbundled network element migration costs, increased costs associated with the acquisition of Cavalier, increased costs associated with equipment sales due to the June 2010 acquisition of Quagga Corporation, and costs incurred to procure electricity from market operators on a wholesale basis, the effects of which were partially offset by a decline in the rates associated with variable usage.

Leased transport charges increased to $613.0 million, or 75.8% of cost of sales, for 2010 from $610.6 million, or 78.0% of cost of sales, for 2009.

Usage costs for local and long distance calls decreased to $120.9 million, or 14.9% of cost of sales, for 2010 from $131.0 million, or 16.7% of cost of sales, for 2009. The decrease was primarily attributable to a decline in the average usage rates PAETEC is charged by network providers.

Cost of sales as a percentage of total revenue increased slightly from 49.5% for 2009 to 49.8% for 2010.

Selling, General and Administrative Expenses. Selling, general and administrative expenses increased to $559.7 million for 2010 from $559.5 million for 2009 primarily due to costs associated with higher staffing levels in PAETEC s sales force and additional growth in headcount from acquisitions during 2010. The impact of these factors was substantially offset by a decrease in stock-based compensation. Selling, general and administrative expenses as a percentage of total revenue decreased to 34.5% for 2010 from 35.4% for 2009, due to initiatives initiated by management during 2010 to align costs more closely with revenue performance and expectations.

Acquisition, Integration and Separation Costs. During 2010, PAETEC recognized approximately $14.1 million of acquisition, integration and separation costs. These costs included acquisition related advisory, legal, accounting, valuation, and other professional fees, as well as costs incurred in connection with employee separations.

Depreciation and Amortization. Depreciation and amortization expense increased to $196.5 million for 2010 from $184.6 million for 2009. The increase was primarily attributable to PAETEC s network deployment activities.

Debt Extinguishment and Related Costs. During 2010, PAETEC recognized a total of $7.4 million of debt extinguishment and related costs, which represented the elimination of $3.6 million of debt issuance costs and unamortized debt discount associated with the repayment of $240.2 million aggregate principal amount of term loans and $30.0 million aggregate principal amount of revolving loans outstanding under the company s senior secured credit facilities with the proceeds from the January 2010 issuance of $300 million aggregate principal amount of its 8 $^{7}/8$% senior secured notes and $0.8 million of costs related to the termination of its interest rate swap agreement. Approximately $3.0 million represented the elimination of unamortized debt issuance costs associated with a financing commitment for senior secured bridge loans which PAETEC terminated upon completion of its offering of the 9 $^{7}/8$% senior notes in December 2010.

Interest Expense. PAETEC s average outstanding debt balances increased to $1,019.4 million for 2010 from $941.2 million for 2009, as a result of the December 2010 issuance of $450 million aggregate principal amount of the 9 $^{7}/8$% senior notes subject to the exchange offer covered by this prospectus and the January 2010 issuance of $300 million aggregate principal amount of its 8 $^{7}/8$% senior secured notes, which was partially offset by the repayment of the outstanding loans under its senior secured credit facilities from the proceeds of the 8 $^{7}/8$% senior secured notes issuance. Interest expense increased to $96.3 million for 2010 from $74.1 million for 2009 due primarily to an increase in the average outstanding debt balances and an increase in the average annual borrowing rate. The weighted average annual borrowing rate, including the amortization of the debt discount and debt premium but excluding the amortization of deferred financing costs, for 2010 was 9.1%, compared to 7.7% for 2009.

Income Taxes. PAETEC completed a reorganization involving some of PAETEC Holding s direct and indirect wholly-owned subsidiaries during 2010. The benefit from income taxes for 2010 reflects the impact to deferred taxes from the reorganization, net of certain current state taxes and income taxes in selected jurisdictions where net operating losses are not available.

PAETEC recorded a benefit from income taxes of $1.0 million for the year ended December 31, 2010, which represented an effective tax rate of 1.7%. The difference between the statutory rate and PAETEC s effective tax rate for the tax year ended December 31, 2010 was primarily attributable to a $6.2 million tax charge to establish a valuation allowance in the current year, the effect of non-deductible stock-based compensation, and the tax impact of the reorganization.

Deferred income tax assets or liabilities reflect temporary differences between amounts of assets and liabilities, including net operating loss, or NOL, carryforwards, for financial and tax reporting. Such amounts are adjusted as appropriate to reflect changes in the tax rates expected to be in effect when the temporary differences reverse. A valuation allowance is established for any deferred income tax asset for which realization is uncertain.

PAETEC considers all available positive and negative evidence, including future reversals of existing temporary differences, projected future taxable income and recent financial operations, to determine whether, based on the weight of that evidence, a valuation allowance is needed for some portion or all of a net deferred income tax asset. Judgment is used in considering the relative impact of negative and positive evidence. In arriving at these judgments, the weight given to the potential effect of negative and positive evidence is commensurate with the extent to which such evidence can be objectively verified. In evaluating the objective evidence that historical results provide, PAETEC considered the past three years of combined results on a pro forma basis, including the results of Cavalier beginning on January 1, 2008.

Based on an assessment of the available positive and negative evidence, including the historical pro forma combined results, PAETEC determined that there are uncertainties relative to its ability to utilize the net deferred income tax assets. In recognition of these uncertainties, PAETEC has provided a valuation allowance of $468.8 million on the net deferred income tax assets as of December 31, 2010. A valuation allowance of $367.9 million existed on the net deferred income tax assets as of December 31, 2009, resulting in a net increase of $100.9 million in the year ended December 31, 2010, of which $6.2 million represents a charge to income tax expense and $94.7 million represents a charge to goodwill as it relates primarily to purchase accounting for the Cavalier acquisition. PAETEC will continue to evaluate the need for a valuation allowance in the future, and if it is determined that its deferred income tax assets are realizable, an adjustment to the valuation allowance will be reflected.

Upon the January 1, 2009 adoption of ASC 805, *Business Combinations*, changes in deferred tax asset valuation allowances and income tax uncertainties after an acquisition date generally will affect income tax expense, including charges and uncertainties associated with acquisitions that closed prior to the effective date of ASC 805.

As of December 31, 2010, PAETEC had federal NOL carryforwards of approximately $1.3 billion, including approximately $262.9 million of NOL carryforwards acquired as part of the December 6, 2010 acquisition of Cavalier. PAETEC has recorded a deferred income tax asset of approximately $519.8 million

Table of Contents

reflecting the benefit of federal and state loss carryforwards. If unused, the NOL carryforwards would expire on various dates from 2016 through 2030. Included in the NOL carryforward deferred tax asset above is approximately $457.4 million of deferred tax assets attributable to federal NOLs and $62.4 million of deferred tax assets attributable to state NOLs. In recognition of the uncertainties relative to the utilization of the NOLs, a full valuation allowance has been recorded.

As a result of the realization requirements of ASC 718*, Compensation Stock Compensation,* PAETEC s deferred tax assets at December 31, 2010 do not include approximately $89.8 million of excess tax benefits from employee stock option exercises that are a component of PAETEC s NOL carryforwards. Equity will be increased by approximately $31.4 million if and when such deferred tax assets are ultimately realized for federal income tax purposes. PAETEC uses ordering pursuant ASC 740, *Income Taxes,* for purposes of determining when excess tax benefits have been realized.

ASC 740 also provides guidance to address uncertainty in tax positions and clarifies the accounting for income taxes by prescribing a minimum recognition threshold, which income tax positions must achieve before being recognized in the financial statements. ASC 740 requires expanded annual disclosures, including a rollforward of the beginning and ending aggregate unrecognized tax benefits as well as specific information related to tax uncertainties for which it is reasonably possible the amount of unrecognized tax benefit will significantly increase or decrease within twelve months. The amount of unrecognized tax benefits from uncertain tax positions, including interest, at December 31, 2010 was $0.8 million, the majority of which, if recognized, would affect the effective tax rate.

2009 Compared With 2008

Revenue. Total revenue increased $9.8 million, or 0.6%, to $1,580.2 million for 2009 from $1,570.4 million for 2008, principally due to a 12.9% increase in PAETEC s data revenue and the inclusion of McLeodUSA s results for the full 2009 period. Of total revenue for 2009, revenue from network services, carrier services and integrated solutions accounted for 79.6%, 16.5% and 3.9%, respectively, compared to 78.8%, 17.3% and 3.9%, respectively, for 2008.

Revenue from network services increased $20.8 million, or 1.7%, to $1,258.5 million for 2009 from $1,237.7 million for 2008. For 2009, revenue from monthly recurring fees and usage-based fees accounted for 72.3% and 26.6%, respectively, of revenue from network services, compared to 71.6% and 27.8%, respectively, of such revenue for 2008. Revenue from core network services accounted for 72.3% of total revenue for 2009, compared to 70.5% for 2008. Revenue from core network services increased $34.3 million, or 3.1%, to $1,141.8 million for 2009 from $1,107.5 million for 2008. The increase in core network services revenue primarily resulted from a 13.0% increase in PAETEC s data revenue generated by increased sales of its Dynamic IP and MPLS VPN products, as well as from the inclusion of McLeodUSA s results for the full 2009 period. Growth of the network services business was affected by lower billable minutes of use, increased pricing pressure, and continued customer attrition, particularly in the non-strategic POTS portion of the business obtained as part of the McLeodUSA acquisition.

Revenue from carrier services decreased $11.3 million, or 4.1%, to $260.0 million for 2009 from $271.3 million for 2008. Revenue from core carrier services accounted for 11.9% of total revenue for 2009, compared to 11.6% for 2008. The decrease in carrier services revenue primarily resulted from a decrease in access fee revenue and reciprocal compensation. For 2009, revenue from monthly recurring fees and usage-based fees accounted for 47.2% and 43.4%, respectively, of revenue from carrier services, compared to 42.0% and 49.9%, respectively, of such revenue for 2008. The increase in monthly recurring fees as a percentage of total carrier services revenue was primarily attributable to the inclusion of McLeodUSA s results for the full 2009 period, as monthly recurring fees historically have represented a higher percentage of total carrier services revenue of McLeodUSA s business than of PAETEC s business.

Table of Contents

Access fee revenue and reciprocal compensation included in network services revenue and access fee revenue and reciprocal compensation included in carrier services revenue together accounted for 8.0% of total revenue for 2009, compared to 8.6% for 2008. Reciprocal compensation revenue included in network services revenue and reciprocal compensation revenue included in carrier services revenue together accounted for 1.2% of total revenue for 2009, compared to 1.6% for 2008. Access fee revenue as a percentage of network services usage-based fees increased to 19.3% for 2009 from 17.7% for 2008, while reciprocal compensation as a percentage of network services usage-based fees increased slightly to 2.1% for 2009 from 2.0% for 2008. Network access fee revenue grew primarily due to the inclusion of McLeodUSA s results for the full 2009 period. Access fee revenue as a percentage of carrier services usage-based fees increased to 37.5% for 2009 from 37.1% for 2008. Reciprocal compensation as a percentage of carrier services usage-based fees decreased to 11.2% for 2009 from 13.2% for 2008. The decrease in reciprocal compensation as a percentage of carrier services usage-based fees was principally attributable to a shift in product mix toward IP-based services and other services that do not generate as much or any reciprocal compensation for PAETEC. PAETEC believes that the decrease also reflected in part adverse economic conditions in PAETEC s markets that have contributed to usage-related pressure experienced by the carrier services business. The carrier services business also experienced a loss of some wireless customers, which PAETEC believes is primarily due to continuing consolidation in the wireless communications industry.

Revenue from integrated solutions services increased $0.2 million, or 0.4%, to $61.7 million for 2009 from $61.4 million for 2008. The increase in revenue generated by the integrated solutions business, which has a longer revenue cycle causing irregular trends on a quarterly basis, was attributable to growth in equipment sales.

Cost of Sales. Cost of sales increased slightly to $782.4 million for 2009 from $781.3 million for 2008, primarily due to the inclusion of McLeodUSA s results for the full 2009 period.

Leased transport charges increased to $610.6 million, or 78.0% of cost of sales, for 2009 from $583.4 million, or 74.7% of cost of sales, for 2008, primarily due to the inclusion of McLeodUSA s results for the full 2009 period.

Usage costs for local and long distance calls decreased to $131.0 million, or 16.7% of cost of sales, for 2009 from $153.2 million, or 19.6% of cost of sales, for 2008. The decrease was attributable in part to a decline in the average usage rates PAETEC is charged by network providers, as well as to a decline in minutes of use.

Cost of sales as a percentage of total revenue decreased slightly from 49.8% for 2008 to 49.5% for 2009.

Selling, General and Administrative Expenses. Selling, general and administrative expenses decreased to $559.5 million for 2009 from $572.2 million for 2008. The decrease was primarily due to a decline in salaries, wages and benefits and a decrease in sales and marketing expenses. The decrease was partially offset by the inclusion of McLeodUSA s results for the full 2009 period, which resulted in an increase in facilities expense to support the company s more extensive network infrastructure after the McLeodUSA acquisition. Selling, general and administrative expenses as a percentage of total revenue decreased to 35.4% for 2009 from 36.4% for 2008.

Sales and Use Tax Settlement. PAETEC recognized a $7.2 million benefit recorded as a sales and use tax settlement in the accompanying consolidated statements of operations and comprehensive (loss) income during the year ended December 31, 2009 as a result of settlement agreements entered into with the Iowa Department of Revenue. These assessments, including estimated interest and penalties, originally amounted to approximately $16.5 million. PAETEC entered into settlement agreements with the Iowa Department of Revenue in April 2009 and January 2010, resolving a substantial portion of the disputed assessments.

Depreciation and Amortization. Depreciation and amortization expense increased to $184.6 million for 2009 from $174.3 million for 2008, largely due to the inclusion of McLeodUSA s results for the full 2009 period.

Table of Contents

Debt Extinguishment and Related Costs. During 2009, PAETEC recognized a total of $17.9 million of debt extinguishment and related costs. In connection with the June 2009 issuance of $300 million aggregate principal amount of its 8 ^{7}/8% senior secured notes, PAETEC recognized $10.3 million of debt extinguishment and related costs, which reflected the elimination of $5.8 million of debt issuance costs and unamortized debt discount related to the repayment of approximately $330.5 million of outstanding term loans under the company s existing senior secured credit facilities and $4.5 million of costs incurred related to the reduction of the notional amount of its swap agreement in effect as of June 30, 2009 from $400.0 million to $265.0 million. PAETEC recognized another $7.5 million of debt extinguishment and related costs in connection with the December 2009 reclassification into earnings of derivative losses previously reported in accumulated other comprehensive loss, due to the discontinuation of hedge accounting treatment of PAETEC s swap agreement in effect as of December 31, 2009.

Interest Expense. PAETEC s average outstanding debt balances increased to $933.2 million for 2009 from $878.2 million for 2008, primarily as a result of the $50.0 million principal amount of loans PAETEC obtained in October 2008 under its revolving credit facility and also as a result of PAETEC s issuance in June 2009 of $300 million aggregate principal amount of its 8^{7}/8% senior secured notes and application of the note proceeds to repay outstanding credit facility term loans. Interest expense increased slightly to $74.1 million for 2009 from $73.7 million for 2008, as the effect of higher debt levels and PAETEC s issuance in June 2009 of its senior secured notes was offset by a decline in the weighted average annual borrowing rates under PAETEC s credit facilities and its notes to 7.6% for 2009 from 7.8% for 2008.

Income Taxes. PAETEC recorded a tax benefit of $1.4 million for the year ended December 31, 2009, which represented an effective tax rate of 4.5%. The difference between the statutory rate and PAETEC s effective tax rate for the tax year ended December 31, 2009 was primarily attributable to a $7.0 million tax charge to establish the valuation allowance on net operating losses generated in the current year, and the effect of non-deductible stock-based compensation.

PAETEC recorded a tax provision of $89.8 million for 2008, which represented an effective tax rate of (22)%. The difference between the statutory rate and PAETEC s effective tax rate for the tax year ended December 31, 2008 was primarily attributable to a $355.0 million non-deductible goodwill impairment charge, a $104.3 million tax charge to establish a valuation allowance, and the effect of non-deductible stock-based compensation.

Based on an assessment of the available positive and negative evidence, including the historical pro forma combined results, PAETEC determined that there are uncertainties relative to its ability to utilize the net deferred tax assets. In recognition of these uncertainties, PAETEC provided a valuation allowance of $367.9 million on the net deferred income tax assets as of December 31, 2009. A valuation allowance of $368.2 million existed on the net deferred income tax assets as of December 31, 2008, resulting in a net decrease of $0.3 million in the year ended December 31, 2009, of which $7.0 million represented a charge to income tax expense and the offsetting $7.3 million decrease to equity.

As of December 31, 2009, PAETEC had federal NOL carryforwards of approximately $962.7 million, including approximately $300.0 million of NOL carryforwards acquired as part of the February 8, 2008 merger with McLeodUSA. PAETEC recorded a deferred income tax asset of approximately $381.4 million reflecting the benefit of federal and state loss carryforwards. If unused, the NOL carryforwards would expire on various dates from 2016 through 2029. In recognition of the uncertainties relative to the utilization of the federal NOLs, a full valuation allowance has been recorded.

Included in the NOL carryforward deferred tax asset above was approximately $44.4 million of deferred tax assets attributable to state NOLs. Management believes that it is more likely than not that the benefit from certain state NOL carryforwards will not be realized prior to their expiration. In recognition of this uncertainty, PAETEC provided a valuation allowance of $43.8 million on the deferred tax assets related to the state NOL carryforwards.

Table of Contents

As a result of the realization requirements of ASC 718*, Compensation Stock Compensation,* PAETEC s deferred tax assets at December 31, 2009 do not include approximately $89.7 million of excess tax benefits from employee stock option exercises that are a component of PAETEC s NOL carryforwards. Equity will be increased by approximately $31.4 million if and when such deferred tax assets are ultimately realized for federal income tax purposes.

The amount of unrecognized tax benefits from uncertain tax positions, including interest, at December 31, 2009 was $0.6 million, the majority of which, if recognized, would affect the effective tax rate.

Critical Accounting Policies

PAETEC s consolidated financial statements are prepared in accordance with generally accepted accounting principles, which require PAETEC to make estimates and assumptions. Of PAETEC s significant accounting policies described in Note 2 to PAETEC s audited consolidated financial statements appearing elsewhere in this prospectus, PAETEC believes that the following policies may involve a higher degree of judgment and complexity.

Revenue Recognition. PAETEC generates recurring operating revenue pursuant to contracts with PAETEC s customers and non-recurring revenue pursuant to non-recurring agreements. PAETEC recognizes revenue in accordance with generally accepted accounting principles, which require satisfaction of the following four basic criteria before revenue can be recognized:

- there is persuasive evidence that an arrangement exists;
- delivery has occurred or services have been rendered;
- the fee is fixed or determinable; and
- collectibility is reasonably assured.

PAETEC bases its determination of the third and fourth criteria above on the company s judgment regarding the fixed nature of the fee it has charged for the services rendered and products delivered, and the prospects that those fees will be collected. If changes in conditions should cause it to determine that these criteria likely will not be met for some future transactions, revenue recognized for any reporting period could be materially adversely affected.

Management makes estimates of future customer credits through the analysis of historical trends and known events. The provisions for revenue adjustments are recorded as a reduction of revenue when incurred. Since any revenue allowances are recorded as an offset to revenue, any future increases or decreases in the allowances will positively or negatively affect revenue by the same amount.

Network Services and Carrier Services Revenue. PAETEC derives revenue primarily from its sale of communications services. PAETEC s service revenue consists principally of usage fees and monthly recurring fees.

Usage fees consist of fees paid by PAETEC s customers for each call made, fees paid by the incumbent carriers in PAETEC s markets as reciprocal compensation when the company terminates non-toll calls originated by their customers, and access fees paid by carriers for long distance calls that PAETEC originates and terminates. PAETEC recognizes revenue related to usage fees when the service is provided. PAETEC bills usage fees in arrears and uses estimates to recognize revenue for unbilled usage fees. PAETEC s ability to generate reciprocal compensation revenue and access revenue is subject to numerous regulatory and legal proceedings. Until these proceedings are ultimately resolved, PAETEC s policy is to recognize reciprocal compensation and access revenue only when it concludes that its realization of that revenue is reasonably assured.

Table of Contents

Monthly recurring fees include the fees paid by PAETEC s customers for lines in service and additional features on those lines. Monthly recurring fees are paid by PAETEC s end-user customers and are billed in advance. PAETEC recognizes this revenue during the period in which it is earned.

PAETEC has arrangements where it recognizes revenue in accordance with ASC 605-20, *Revenue Recognition Services*, which requires some non-recurring service activation and installation fee revenues that are payable in advance of the provision of services to be deferred over the average customer life. In accordance with those guidelines, PAETEC defers service activation and installation fee revenues and related costs and amortizes them over the average customer life, which is primarily three years.

PAETEC also derives revenue from sales of indefeasible rights to use fiber optic telecommunications network facilities, or IRUs, and telecommunications network maintenance arrangements on such IRUs. The revenue from IRUs is recognized over the term of the related lease unless it qualifies as a sales type lease, for which revenue is recognized at the time the sale criteria in ASC 605-976, *Real Estate Retail Land*, are met. Base annual revenue for telecommunications network maintenance is recognized on a straight-line basis over the term of the contract. Additional services provided under these contracts are recognized as the services are performed.

Integrated Solutions Revenue. PAETEC also derives revenue from sales of telecommunications equipment, software and energy supply services. Equipment revenue consists of fees PAETEC s customers pay for equipment and for PAETEC s system design and installation services. PAETEC recognizes equipment revenue upon delivery and acceptance of the equipment. PAETEC derives software revenue through selling and supporting its proprietary telecommunications software. PAETEC recognizes revenue related to software sales upon delivery and acceptance of the software in accordance with ASC 605-985, *Software*. Support fees include fees for maintenance of PAETEC s telecommunications software and fees for training the end user in the proper use of PAETEC s telecommunications software. PAETEC recognizes maintenance fees pro rata over the length of the underlying maintenance contract. PAETEC recognizes training fees after the training obligation has been fulfilled. Energy revenue is derived through the sale of energy supply services. PAETEC recognizes revenue related to energy sales when the service is provided.

Allowance for Doubtful Accounts. To determine its allowance for bad debts, PAETEC uses estimates based on the company s historical collection experience, its assessment of current industry and economic trends, its customer concentrations and its credit policies. As of March 31, 2011, PAETEC had reserved for $12.7 million of bad debts.

PAETEC has reserved for expected bad debt losses based on the factors referred to above, and believes that its reserves are adequate. It is possible, however, that the sufficiency of PAETEC s estimates could become materially inadequate as the composition of PAETEC s receivables changes over time. PAETEC continually reviews and refines the estimation process to take account of these changes, but from time to time the company may need to adjust its estimate to reflect actual experience.

Cost of Sales. Costs of sales are composed primarily of network costs, which are costs incurred for leased transport charges and for transmission of voice and data services over other carriers networks. These costs consist of both fixed payments and variable amounts based on actual usage and negotiated or regulated contract rates. PAETEC expenses network costs as incurred. These costs include PAETEC s estimate of charges for which it has not yet received bills, and are based upon the estimated number of transmission lines and facilities PAETEC has in service and its estimated minutes of use based on internal reports. Once PAETEC receives an invoice from a carrier, the company begins a process of reconciling that carrier s invoice to PAETEC s internal reports. Once the reconciliation is complete, PAETEC follows contractual terms to dispute any erroneous billing and, ultimately, agrees with the carrier on the final amount due. In some cases, this reconciliation process can take several months to complete. PAETEC may make subsequent adjustments to its estimates after it receives bills for the actual costs it incurs, but PAETEC generally does not expect that these adjustments will be material to its operating results. Accordingly, PAETEC s accrual for network costs includes estimates for which the reconciliation of the carriers invoices to PAETEC s internal reports has not been completed. Because of the significance of access costs, the complexity of the systems that capture accrual information, and the quantity of negotiated and regulated rates, PAETEC believes that the estimation of network cost accruals is a critical accounting policy. As of December 31, 2010 and 2009, PAETEC had $36.2 million and $27.8 million, respectively, of disputed network invoices and approximately $4.7 million and $8.1 million, respectively, of recorded reserves related to disputed balances recorded in accounts payable on the consolidated balance sheets. As of March 31, 2011, PAETEC had approximately $34.9 million of disputed network invoices and approximately $4.5 million of recorded reserves related to that disputed balance recorded in accounts payable on the consolidated balance sheet.

Impairment of Long-Lived Assets and Finite-Lived Intangible Assets. It is PAETEC s policy to review its long-lived assets for possible impairment whenever events or circumstances indicate that the carrying amount of an asset may not be recoverable. Factors the company considers important, and which could trigger an impairment review, include the following:

- significant under-performance of PAETEC s assets relative to expected historical or projected future operating results;
- significant changes in the manner in which PAETEC uses its assets or significant changes in PAETEC s overall business strategy;
- significant negative industry or economic trends; and
- a significant decline in fair market value of PAETEC s common stock for a sustained period.

PAETEC determines whether the carrying value of its long-lived assets, including property and equipment, and finite-lived intangible assets may not be recoverable based upon the existence of one or more of the foregoing or other indicators of impairment. PAETEC determines if impairment exists relating to long-lived assets by comparing future undiscounted cash flows to the asset s carrying value. If the carrying value is greater than the undiscounted cash flows, PAETEC measures the impairment as the amount by which the carrying value of the assets exceeds the fair value of the assets. Because of the significance of long-lived assets and finite-lived intangible assets and the judgments and estimates that go into the fair value analysis, PAETEC believes that its policies regarding impairment are critical.

Goodwill and Indefinite-Lived Intangible Assets. In accordance with the provisions of ASC 350, *Goodwill and Other Intangible Assets*, PAETEC does not amortize goodwill or other acquired intangible assets with indefinite useful lives. PAETEC has identified two reporting units as defined in ASC 350. As of December 31, 2010 and 2009, PAETEC had $439.6 and $300.6 million of goodwill, respectively, with the telecommunications reporting unit accounting for approximately 99% of such goodwill as of the same dates. As of December 31, 2010 and 2009, PAETEC had $2.4 million of intangible assets with indefinite lives, respectively.

Goodwill is assessed for impairment at least annually using a two-step impairment test. Step one of the test is used to identify whether or not impairment may exist. In step one, PAETEC compares the fair value of each individual reporting unit with its carrying amount. PAETEC estimates the fair value of its reporting units based on the income approach, using a discounted projection of future cash flows, supported with a market-based valuation. The income approach is dependent on a number of critical management assumptions, including estimates of future cash flows that take into account assumed growth rates, price increases, profitability margins, capital expenditures, benefits of recent acquisitions and expected synergies, and an appropriate discount rate. PAETEC s estimates of discounted cash flows may differ from actual cash flows due to, among other factors, economic conditions, changes to PAETEC s business model or changes in operating performance. Significant differences between these estimates and actual cash flows could materially affect PAETEC s future financial results. If a reporting unit s carrying amount exceeds its fair value, impairment may exist. Step two of the impairment test must then be performed to measure the amount of impairment, if any. Goodwill impairment potentially exists when the implied fair value of a reporting unit s goodwill is less than its carrying value. ASC 350 requires PAETEC to determine the implied fair value of goodwill in the same manner as if PAETEC had acquired those reporting units. Specifically, PAETEC allocates the fair value of the reporting unit to the assets, including any unrecognized intangible assets, and liabilities of that reporting unit, in a hypothetical calculation that yields the implied fair value of the goodwill. If the carrying amount of the reporting unit s goodwill is greater than the implied fair value of its goodwill, an impairment loss must be recognized for the excess.

PAETEC assesses the carrying value of its goodwill during the third quarter of each fiscal year. The annual assessment of the carrying value of PAETEC s reporting units undertaken with respect to 2010, 2009 and 2008 indicated that goodwill was not impaired as of July 1, 2010, 2009 and 2008, respectively.

In accordance with ASC 350, goodwill of a reporting unit will also be tested for impairment between annual tests if a triggering event occurs, as defined by ASC 350, which could potentially reduce the fair value of the reporting unit below its carrying value. During the third quarter of 2008, PAETEC experienced a significant decline in market capitalization as a result of a decrease in the market price of its common stock as reported on the NASDAQ Global Select Market. The decline in market capitalization occurred after PAETEC s announcement in August 2008 that its operating results for the second quarter of 2008 would be lower than expected. Some factors contributing to this performance below expectations included less robust billable minutes of use, an increase in customer attrition rates, and continued pricing pressures resulting from competitive product offerings and customer demands for price reductions in connection with contract renewals. PAETEC determined that these factors combined with the overall general decline in the economy and financial markets were an indicator that a goodwill impairment test was required pursuant to ASC 350. As a result, PAETEC completed step one of the impairment process and concluded that the fair values of some of its reporting units were less than the carrying values. For those reporting units whose fair values were less than the carrying values, PAETEC conducted step two of the impairment process and determined that the fair value of each reporting unit s goodwill was less than the carrying value and concluded that goodwill was impaired. PAETEC recorded a non-cash goodwill impairment charge of $340.0 million in the third quarter of 2008 based on a preliminary assessment. In the fourth quarter of 2008, management finalized the assessment in connection with the preparation of the company s audited financial statements and recorded an additional non-cash charge of $15.0 million. Approximately 95% of the goodwill impairment charge was attributed to the telecommunications reporting unit. The $355.0 million impairment charge is representative of the cumulative impairment charges since PAETEC adopted ASC 805.

During the fourth quarter of 2008, PAETEC s market capitalization declined further as a result of a decrease in the market price of its common stock as reported on the NASDAQ Global Select Market from the market price at September 30, 2008. PAETEC determined that the continued decline in market capitalization and the continuation of the factors that were identified during the third quarter of 2008 were an indicator that a goodwill impairment test was again required pursuant to ASC 350 for the fourth quarter of 2008. As a result, PAETEC completed step one of the impairment process and concluded that the fair values of its reporting units exceeded the carrying values and therefore recorded no impairment.

The changes in the carrying value of goodwill from January 1, 2009 through March 31, 2011 were as follows (in thousands):

Balance as of January 1, 2009 and December 31, 2009	$ 300,597
Goodwill related to the acquisition of Cavalier	112,363
Goodwill related to other acquisitions	26,596
Balance as of December 31, 2010	$ 439,556
Goodwill related to other acquisitions	4,237
Balance as of March 31, 2011	$ 443,793

Share-Based Payment. Employees of PAETEC participate in various equity incentive plans. In accordance with ASC 718, *Compensation Stock Compensation*, PAETEC measures the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. PAETEC recognizes these compensation costs ratably over the period during which an employee is required to provide service in exchange for the award. The fair value of each option award is estimated on the date of grant using the Black-Scholes option-pricing model that uses assumptions regarding expected volatilities based on historical experience. The expected term of options granted is derived from the vesting period of the award, as well as exercisability of the award, and represents the period of time that options granted are expected to be outstanding. The risk-free rate is calculated using the U.S. Treasury yield curve, and is based on the expected term of the option. PAETEC uses historical data to estimate forfeitures.

The assumptions used in calculating the fair value of share-based payment awards represent management s best estimates, but these estimates involve inherent uncertainties and the application of management judgment. As a result, if factors change and PAETEC uses different assumptions, its stock-based compensation expense could be materially different in the future. In addition, PAETEC is required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. If PAETEC s actual forfeiture rate is materially different from its estimate, the stock-based compensation expense could be significantly different from the amount recorded by PAETEC in the current period.

Income Taxes. PAETEC accounts for income taxes in accordance with ASC 740, *Income Taxes*. The asset and liability approach underlying ASC 740 requires the recognition of deferred income tax liabilities and assets for the expected future tax consequences of temporary differences between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. Management provides valuation allowances against the net deferred income tax asset for amounts that are not considered more likely than not to be realized.

PAETEC considers all available evidence, both positive and negative, to determine whether, based on the weight of that evidence, a valuation allowance is needed for some portion or all of a net deferred income tax asset. PAETEC uses judgment in considering the relative impact of negative and positive evidence. In arriving at these judgments, the weight given to the potential effect of negative and positive evidence is commensurate with the extent to which such evidence can be objectively verified.

Business Combinations. PAETEC accounts for businesses acquired subsequent to January 1, 2009 using the acquisition method of accounting. Under this method, all acquisition-related costs are expensed as incurred. PAETEC records the underlying net assets at their respective acquisition-date fair values. As part of this process, PAETEC identifies and attributes values and estimated lives to property and equipment and intangible assets acquired. These determinations involve significant estimates and assumptions, including those with respect to future cash flows, discount rates and asset lives, and therefore require considerable judgment. These determinations affect the amount of depreciation and amortization expense recognized in future periods. The results of operations of acquired businesses are included in the consolidated statement of operations beginning on the respective business s acquisition date.

Previously, PAETEC accounted for businesses acquired using the purchase method of accounting. PAETEC allocated the total cost of an acquisition, including certain acquisition-related costs, to the underlying net assets based on their respective estimated fair values.

Derivatives. ASC 815, *Derivatives and Hedging*, allows the gains and losses of a derivative to offset related results on the hedged item in the consolidated statements of operations and comprehensive loss, and requires PAETEC formally to document, designate and assess the effectiveness of transactions that receive hedge accounting.

Derivatives are recognized on the consolidated balance sheet at fair value. PAETEC s freestanding derivative instruments are designated as hedges at inception and evaluated for effectiveness at least quarterly throughout the hedge period. These derivatives are designated as hedges of the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge). The effective portion of the derivative s gain or loss is initially reported as a component of comprehensive income and subsequently reclassified into earnings when the forecasted transaction affects earnings. The ineffective portion of the gain or loss is reported in earnings immediately.

PAETEC formally documents all relationships between hedging instruments and hedged items, as well as the risk-management objective and strategy for undertaking various hedge transactions. This process includes linking all derivatives that are designated as cash flow hedges to specific assets and liabilities on the balance sheet.

PAETEC discontinues hedge accounting prospectively when it determines that the derivative is no longer effective in offsetting changes in cash flows of a hedged item, the derivative or hedged item expires or is sold, terminated, or exercised, or management determines that it is no longer appropriate to designate the derivative as a hedge instrument.

Legal and Contingency Reserves. PAETEC accounts for legal and other contingencies in accordance with ASC 450, *Contingencies*. Loss contingencies are accrued by a charge to income if both of the following conditions are met: information before issuance of the financial statements indicates that it is probable that an asset has been impaired or a liability has been incurred at the date of the financial statements; and the amount of the loss can be reasonably estimated.

The foregoing list of critical accounting policies is not intended to be a comprehensive list of all of PAETEC s accounting policies. In many cases, the accounting treatment of a particular transaction is specifically dictated by accounting principles generally accepted in the United States of America, with no need for PAETEC to judge their application. There are also areas in which PAETEC s judgment in selecting any available alternative would not produce a materially different result. In addition to reviewing the foregoing list, PAETEC encourages you to review carefully the notes to its audited consolidated financial statements appearing elsewhere in this prospectus, where you will find a more comprehensive description of the company s accounting policies and additional disclosures that are required by generally accepted accounting principles.

Liquidity and Capital Resources

PAETEC finances its operations and growth primarily with cash flow from operations, issuances of debt securities and other loans, operating leases and normal trade credit terms.

Sources and Uses of Cash. PAETEC s cash flows for the three months ended March 31, 2011 and 2010, respectively, were as follows (in thousands):

	Three Months Ended March 31, 2011	2010
Net cash provided by operating activities	$ 60,685	$ 7,828
Net cash used in investing activities	$ (49,331)	$ (34,997)
Net cash (used in) provided by financing activities	$ (3,034)	$ 18,561

The $52.9 million increase in cash flows from operating activities for the 2011 quarter over the 2010 quarter was primarily attributable to a $11.6 million increase in net loss adjusted for non-cash items and a $41.2 million increase in working capital.

PAETEC s investing activities during the 2011 and 2010 quarters consisted primarily of activities related to the purchase of property and equipment. Investing activities during the 2010 quarter also included the acquisition of U.S. Energy Partners LLC.

Table of Contents

Net cash used in financing activities of $3.0 million for the 2011 quarter was primarily related to repayments of long-term debt. Net cash provided by financing activities of $18.6 million for the 2010 quarter was primarily related to the January 2010 issuance and sale of $300.0 million aggregate principal amount of the 8 7/8% senior secured notes, partially offset by the payment of debt issuance costs incurred in connection with such sale. PAETEC applied a portion of the proceeds from the January 2010 sale of the 8 7/8% senior secured notes to repay $240.2 million aggregate principal amount of term loans and $30.0 million aggregate principal of revolving loans outstanding under its senior secured credit facilities.

PAETEC s cash flows for 2010, 2009 and 2008 were as follows (in thousands):

	Years Ended December 31,		
	2010	2009	2008
Net cash provided by operating activities	$ 125,768	$ 152,169	$ 152,131
Net cash used in investing activities	$ (621,894)	$ (119,748)	$ (227,971)
Net cash provided by (used in) financing activities	$ 438,771	$ (44,061)	$ 127,767

The $26.4 million decrease in cash flows from operating activities for 2010 compared to 2009 was primarily attributable to a $27.4 million decrease in net income adjusted for non-cash items, which was offset by a $1.0 million increase in working capital. Cash flows from operating activities for 2009 were consistent with those for 2008, with a $33.3 million increase in net income adjusted for non-cash items being offset by a $33.3 million decrease in working capital.

PAETEC s investing activities for 2010 consisted primarily of activities related to the acquisition of Cavalier and the purchase and installation of property and equipment. PAETEC s investing activities for 2009 consisted primarily of activities related to the purchase and installation of property and equipment. PAETEC s investing activities for 2008 consisted primarily of activities related to the acquisition of McLeodUSA and the purchase and installation of property and equipment.

Net cash provided by financing activities of $438.8 million for 2010 was primarily related to the January 2010 issuance and sale of $300.0 million aggregate principal amount of the 8 7/8% senior secured notes and the December 2010 issuance and sale of $450 million aggregate principal amount of the 9 7/8% senior notes subject to the exchange offer covered by this prospectus by a wholly-owned subsidiary of PAETEC Holding and the subsequent assumption by PAETEC Holding of the subsidiary s obligations and agreements in respect of the 9 7/8% senior notes. The effects of these note issuances were partially offset by the payment of debt issuance costs incurred in connection with each sale. See Indebtedness below for information about the application of the proceeds of these note issuances. Net cash used in financing activities of $44.1 million for 2009 was primarily related to the repayment of $330.5 million aggregate principal amount of borrowings under PAETEC s senior secured credit facilities with the proceeds of its June 2009 offering of $350 million aggregate principal amount of its 8 7/8% senior secured notes, the payment of debt issuance costs incurred in connection with such sale, and the repayment of $20.0 million aggregate principal amount of loans outstanding under PAETEC s revolving credit facility. Net cash provided by financing activities for 2008 of $127.8 million was primarily related to $100 million of borrowings incurred under PAETEC s incremental term loan facility, a portion of which was applied toward the redemption of McLeodUSA s outstanding senior secured notes in connection with the McLeodUSA acquisition, and $50.0 million of borrowings under PAETEC s revolving credit facility.

Contractual Obligations and Commitments. PAETEC has various contractual obligations and commercial commitments. PAETEC does not have off-balance sheet financing arrangements other than its letters of credit and operating leases. As of March 31, 2011, PAETEC was party to letters of credit totaling $8.0 million. PAETEC does not expect any material losses from the resolution of these letters of credit since performance is not likely to be required.

Table of Contents

The following table sets forth, as of December 31, 2010, PAETEC s future contractual obligations and commercial commitments:

Contractual Obligations

(in thousands)

	Total	Less Than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Long-term debt	$ 1,425,530	$ 130	$ 25,165	$ 300,043	$ 1,100,192
Capital lease obligations	45,805	10,603	27,270	5,931	2,001
Operating leases	203,220	40,685	65,399	41,843	55,293
Purchase obligations	180,413	144,866	31,950	3,597	
Other long-term liabilities	78,822		27,116	14,714	36,992
Total	$ 1,933,790	$ 196,284	$ 176,900	$ 366,128	$ 1,194,478

The long-term debt obligations in the table above do not include scheduled interest payments on the $25 million aggregate principal amount under PAETEC s variable-rate revolving credit facility outstanding at December 31, 2010, which are generally based on the London interbank offered rate, or LIBOR, and on the $1,400 million aggregate principal amount under PAETEC s senior notes and senior secured notes outstanding at December 31, 2010. PAETEC projects interest payments on such indebtedness to be $136.1 million for fiscal 2011, $135.5 million for fiscal 2012, $135.4 million for fiscal 2013 and 2014, $119.7 million for fiscal 2015, and $216.1 million thereafter.

Indebtedness. At March 31, 2011, PAETEC had approximately $1,447.1 million of total indebtedness, net of an unamortized discount of $22.5 million. The overall weighted average annual interest rate, including the amortization of the debt discount and debt premium but excluding deferred financing costs, was 9.4%. Of this total indebtedness, an aggregate principal amount of $300.0 million was outstanding under the 9.5% senior notes, an aggregate principal amount of $650.0 million was outstanding under 8 7/8% senior secured notes, an aggregate principal amount of $450.0 million was outstanding under the 9 7/8% senior notes subject to the exchange offer covered by this prospectus, an aggregate principal amount of $25.0 million was outstanding under the company s revolving credit facility, and an aggregate of $44.6 million consisted of capital leases and other indebtedness.

As of March 31, 2011, PAETEC s senior secured credit facilities available pursuant to its credit agreement consisted of the following:

- a term loan credit facility under which no term loans were outstanding and under which PAETEC could obtain incremental term loans, subject to conditions, in an aggregate principal amount of up to approximately $65.0 million under one or more incremental facilities; and

- a revolving credit facility under which PAETEC could obtain from time to time revolving loans of up to an aggregate principal amount of $50.0 million outstanding at any time, of which $25.0 million principal amount of revolving loans were outstanding.

Under the terms of the total leverage ratio covenant contained in PAETEC s credit agreement for its senior credit facilities, PAETEC s ratio of consolidated debt to consolidated adjusted EBITDA (as defined for purposes of the credit agreement) as of any measurement date will not be permitted to be greater than 5.00:1.00. PAETEC was in compliance with this financial covenant as of March 31, 2011.

On April 12, 2011, PAETEC announced that it will seek $225 million aggregate principal amount of new senior secured credit facilities to replace its existing credit facilities. The new credit facilities will consist of a five-year senior secured revolving credit facility in an aggregate principal amount of $125 million and a seven-year senior secured term loan facility in an aggregate principal amount of $100 million. The proceeds from

borrowings under the new credit facilities will be used for general corporate purposes, including repayment of

59

Table of Contents

the $25 million principal amount of borrowings outstanding under PAETEC s existing senior secured revolving credit facility and to complete the recently announced acquisition of XETA Technologies, Inc., the closing of which is subject to customary closing conditions. PAETEC s ability to obtain the new credit facilities on terms that are acceptable to it will be subject to market conditions and customary closing conditions.

See Note 6 to PAETEC s audited consolidated financial statements appearing elsewhere in this prospectus for additional information regarding the company s indebtedness.

Operating Lease Obligations. PAETEC has entered into various non-cancelable operating lease agreements, with expiration dates through 2030, for office space and equipment. Some of these leases have free or escalating rent payment provisions. PAETEC recognizes rent expense under these leases on a straight-line basis. The company began occupying its current corporate headquarters in January 2001 under a 20-year lease agreement. PAETEC expects that its annual rental payments under the lease will increase to approximately $2.0 million for the last ten years of the lease term. PAETEC s rental payments under the lease were $2.0 million for 2010.

In December 2010, PAETEC entered into an agreement with the city of Rochester, New York, under which PAETEC will purchase from the city a parcel of land in downtown Rochester and construct a new headquarters building for an estimated total cost of approximately $54 million. The agreement is subject to numerous conditions, contingencies, and approvals, including the receipt of various forms of governmental financial subsidies.

Purchase Obligations. PAETEC s purchase obligations as of March 31, 2011 represent non-cancelable contractual obligations for equipment and services and minimum commitments under data and voice contracts with certain carriers.

Other Long-Term Liabilities. Included in PAETEC s long-term liabilities as of March 31, 2011, the majority of which the company anticipates will not require payments during the periods presented or thereafter, are deferred revenues, tax contingency reserve and deferred rent credits.

Stock Repurchase Program. In 2009, PAETEC Holding s board of directors authorized the repurchase of up to $25.0 million of PAETEC Holding s outstanding common stock through December 31, 2010, subject to conditions. PAETEC Holding was permitted to repurchase shares from time to time, at its discretion, on the open market or in private transactions. The repurchase program did not obligate PAETEC Holding to repurchase any specific number of shares.

During 2010, PAETEC Holding repurchased, at fair market value and on the open market, a total of 4,033,036 shares of its common stock at a total cost of approximately $16.1 million. In connection with the repurchases, PAETEC Holding paid commissions totaling approximately $0.1 million. The authorized stock repurchase program expired on December 31, 2010.

Capital and Cash Requirements. PAETEC expects that it will continue to require significant capital expenditures to maintain and enhance its network and services and to generate planned revenue growth. PAETEC made capital expenditures, principally for the purchase of communications equipment, of approximately $46.8 million in the 2011 quarter. PAETEC expects to fund all of its 2011 capital expenditures from cash on hand and cash flow from operations. PAETEC plans to make such capital expenditures primarily for the following purposes:

- to continue to acquire and install equipment to enhance and maintain its network;
- to increase penetration of its existing markets;
- to expand its operations into additional geographic markets; and
- to make infrastructure enhancements, principally for its back office systems.

Table of Contents

The actual amount and timing of PAETEC s capital requirements may differ materially from its estimates as a result of regulatory, technological and competitive developments in the company s industry. As of March 31, 2011, PAETEC had entered into agreements with vendors to purchase approximately $169.6 million of equipment and services, of which the Company expects $136.7 million to be delivered and payable in the year ending December 31, 2011, $15.1 million to be delivered and payable in the year ending December 31, 2012, $15.1 million to be delivered and payable in the year ending December 31, 2013, and the remaining $2.7 million to be delivered and payable in the year ending December 31, 2014.

PAETEC may seek to purchase from time to time some of its outstanding senior notes and/or some of its outstanding senior secured notes for cash in open market transactions, privately negotiated transactions or otherwise. Such repurchases, if any, will depend on prevailing market conditions and the discount, if any, at which the notes may be purchased, PAETEC s liquidity requirements, contractual restrictions and other factors. The amounts involved in any such purchases may be material.

PAETEC believes that cash on hand and cash flow from operations, and amounts expected to be available under its revolving credit facility will provide sufficient cash to enable the company to fund its planned capital expenditures, make scheduled principal and interest payments on its debt, meet its other cash requirements, and maintain compliance with the terms of its financing agreements for at least the next 12 months. After the foregoing period, PAETEC may require additional capital for network enhancements to provide increased capacity to meet expected increased demand for its services. The amount and timing of these additional network enhancements, if any, will depend on the anticipated demand for services, the availability of funds and other factors. The actual amount and timing of PAETEC s future capital requirements may differ materially from the company s estimates depending on the demand for its services and new market developments and opportunities, and on other factors, including those described in this prospectus under Risk Factors. If PAETEC s plans or assumptions change or prove to be inaccurate, the foregoing sources of funds may prove to be insufficient. In addition, if PAETEC seeks to acquire other businesses or to accelerate the expansion of its business, it may be required to seek material amounts of additional capital. Additional sources may include equity and debt financing and other financing arrangements, such as vendor financing. Further, if PAETEC believes it can obtain additional debt financing on advantageous terms, PAETEC may seek such financing at any time, to the extent that market conditions and other factors permit it to do so. The debt financing PAETEC may seek could be in the form of additional term loans under its existing or new senior secured credit facilities or additional debt securities having substantially the same terms as, or different terms from, PAETEC s outstanding senior notes and senior secured notes. Any inability of PAETEC to generate the sufficient funds that it may require or to obtain such funds under reasonable terms could limit its ability to increase its revenue or to operate profitably. PAETEC s ability to raise any required funds is subject to restrictions imposed by covenants contained in its existing debt agreements and could be negatively affected by a continuation of adverse conditions in the credit and capital markets.

Recently Issued Accounting Standards

In October 2009, the FASB issued ASU 2009-13, *Revenue Recognition (Topic 605)*. This ASU provides amendments to the criteria in ASC 605-25 for separating consideration in multiple-deliverable revenue arrangements. It establishes a hierarchy of selling prices to determine the selling price of each specific deliverable, which includes vendor-specific objective evidence (if available), third-party evidence (if vendor-specific evidence is not available), or estimated selling price if neither of the first two is available. This ASU also eliminates the residual method for allocating revenue between the elements of an arrangement and requires that arrangement consideration be allocated at the inception of the arrangement. Finally, this ASU expands the disclosure requirements regarding a vendor s multiple-deliverable revenue arrangements. The adoption of this accounting standard on January 1, 2011 did not have a material impact on PAETEC s financial statements.

In October 2009, the FASB issued ASU 2009-14, *Certain Revenue Arrangements that include Software Elements*. This ASU amends accounting and reporting guidance under ASC 605-985 to exclude from its scope all tangible products containing both software and non-software components that function together to deliver the product s essential functionality. The adoption of this accounting standard on January 1, 2011 did not have a material impact on PAETEC s financial statements.

Quantitative and Qualitative Disclosures about Market Risk

PAETEC is exposed to market risks in the normal course of business. PAETEC manages the sensitivity of its results of operations to these risks by maintaining an investment portfolio consisting primarily of short-term, interest-bearing securities and by entering into long-term debt obligations with appropriate pricing and terms. PAETEC does not hold or issue derivative, derivative commodity or other financial instruments for trading purposes. PAETEC does not have any material foreign currency exposure. PAETEC s major market risk exposure is to changing interest rates associated with borrowings the company uses to fund the expansion of its business and to support its acquisition activities. The interest rates that PAETEC is able to obtain on this debt financing depend on market conditions. PAETEC s policy is to manage interest rates through a combination of fixed-rate debt and, from time to time, the use of interest rate swap contracts to manage the company s exposure to fluctuations in interest rates on variable-rate debt. As of March 31, 2011, the $25.0 million aggregate principal amount outstanding under PAETEC s revolving credit facility accrued interest at floating rates. A change of one percentage point in the interest rates applicable to the balance of PAETEC s variable rate debt would result in a fluctuation of approximately $0.3 million in the company s annual interest expense.

Management s Annual Report on Internal Control Over Financial Reporting

The management of PAETEC Holding Corp. (the Company) is responsible for establishing and maintaining an adequate system of internal control over financial reporting. This system is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with the accounting principles generally accepted in the United States of America.

The Company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and (3) provide reasonable assurance regarding the prevention or timely detection of unauthorized acquisition, use, or disposition of the Company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, a system of internal control over financial reporting can provide only reasonable assurance and may not prevent or detect misstatements. Further, because of changes in conditions, effectiveness of internal control over financial reporting may vary over time. The Company s system contains self-monitoring mechanisms, and actions are taken to correct deficiencies as they are identified.

Management conducted an evaluation of the effectiveness of the system of internal control over financial reporting based on the framework in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commissions (the COSO Framework). Based on this evaluation, management concluded that the Company s system of internal control over financial reporting was effective as of December 31, 2010, based on the COSO Framework. Management has excluded from the scope of its assessment of internal control over financial reporting the operations and related assets of U.S Energy Partners LLC (U.S. Energy), Quagga Corporation (Quagga), and Cavalier Telephone Corporation and its subsidiaries (collectively, Cavalier), which the Company acquired on February 28, 2010, June 7, 2010 and December 6, 2010, respectively. At December 31, 2010 and for the period from March 1, 2010 through December 31, 2010,

Table of Contents

total assets and total revenues subject to U.S. Energy s internal control over financial reporting represented 0.7% and 1.5% of the Company s consolidated total assets and consolidated total revenues, respectively, as of December 31, 2010 and for the year ended December 31, 2010. At December 31, 2010 and for the period from June 8, 2010 through December 31, 2010, total assets and total revenues subject to Quagga s internal control over financial reporting represented 2.1% and 1.3% of the Company s consolidated total assets and consolidated total revenues, respectively, as of December 31, 2010 and for the year ended December 31, 2010. At December 31, 2010 and for the period from December 6, 2010 through December 31, 2010, total assets and total revenues subject to Cavalier s internal control over financial reporting represented 28.3% and 1.4% of the Company s consolidated total assets and consolidated total revenues, respectively, as of December 31, 2010 and for the year ended December 31, 2010.

Deloitte & Touche LLP, an independent registered public accounting firm, has audited the effectiveness of PAETEC s internal control over financial reporting, as stated in its report which is included herein.

PAETEC Holding Corp.

March 16, 2011	By:	/s/ Arunas A. Chesonis
	Name:	**Arunas A. Chesonis**
	Title:	**Chairman, President and Chief Executive Officer** **(Principal Executive Officer)**
March 16, 2011	By:	/s/ Keith M. Wilson
	Name:	**Keith M. Wilson**
	Title:	**Executive Vice President and Chief Financial Officer** **(Principal Financial Officer)**

63

BUSINESS

PAETEC is a competitive broadband communications services and solutions provider guided by the principle that delivering superior customer service is the key to competing successfully with other communications services providers. PAETEC s primary business is providing business end-user customers in metropolitan areas with a package of integrated broadband communications services that encompasses data services, including Internet access services and virtual private network services, and voice services, including local telephone services and domestic and international long distance services. As of March 31, 2011, PAETEC provided services for over 54,000 business customers in a service area encompassing 86 of the top 100 metropolitan statistical areas.

We maintain a corporate Internet web site at www.paetec.com. We make available free of charge through our web site our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports, as soon as reasonably practicable after we electronically file or furnish the reports with the SEC. The contents of our web site are not a part of this prospectus.

PAETEC s Business

PAETEC provides a range of broadband data and voice network services on a retail basis primarily to business customers. In addition, PAETEC has an existing base of residential customers and expects to continue to expand that base as a result of its acquisition of Cavalier. PAETEC s provision of residential services is not a central part of its business.

PAETEC also offers a range of data and voice carrier services on a wholesale basis to other communications companies and to larger-scale purchasers of network capacity.

PAETEC complements its offering of its network and carrier services with sales to its business customers of integrated solutions, including data center solutions, software applications, network integration services, managed services, energy services and communications equipment. PAETEC also offers these integrated services on a stand-alone basis to its business customers. PAETEC s sales and marketing initiatives focus on bundling its network services and integrated solutions for sale to its customers. PAETEC believes this bundling adds value for its customers and increases its share of its customers expenditures on broadband communications services.

As of March 31, 2011, PAETEC delivered its communications services in 48 states and the District of Columbia, had broadband network and facilities spanning approximately 36,700 route miles and operated 166 switching facilities that provide traditional voice and Internet Protocol capabilities.

PAETEC has designed its network, developed its back office systems and trained its employees and sales agents to support a broad line of services. PAETEC believes that its ability to bundle a package of value-added communications services enables it to build customer loyalty, increase the penetration of its existing markets and facilitate its entry into additional markets.

Network Services

PAETEC offers a range of broadband network services and solutions to its retail end-user customers, encompassing both data services, including Internet access services and virtual private network services, and voice services, including local telephone services and domestic and international long distance services. PAETEC derived approximately 76.7% of its total revenue for 2010 from its network services.

Data Services. PAETEC offers its customers the following broadband Internet connectivity and other data services:

High-speed dedicated Internet access services. PAETEC offers integrated voice and broadband Internet access over a single digital transmission line. With this service, PAETEC s customers are able to obtain voice and broadband Internet access services at competitive prices from a single source. PAETEC also offers its high-volume broadband Internet access customers a specialized Internet access service that provides very high speed Internet access.

Virtual private network services. Virtual private networks, or VPNs, are networks that are typically leased and that link multiple customer locations by using computer software to dedicate circuits solely for the customer s use, instead of building a physical circuit to each customer location. PAETEC offers VPN services to businesses seeking a cost-effective means of creating their own secure networks for communicating and conducting business with their employees, customers and suppliers. PAETEC offers its VPN services primarily utilizing multi-protocol label switching, or MPLS.

Internet security services. To supplement its Internet and MPLS VPN data access services, PAETEC offers data encryption services and electronic message screening services on a resale basis to customers that seek to minimize security issues associated with direct Internet access.

Voice Services. PAETEC offers its customers the following local, long distance and other voice services:

Local telephone services. PAETEC s local telephone service offering provides basic local dial tone service, as well as additional services, such as directory assistance, call forwarding and call hunting. PAETEC is certified to offer local telephone services in 48 states and the District of Columbia.

Long distance services. PAETEC offers a range of switched and dedicated long distance services to customers connected to its network. These include services that originate and terminate within the same local transport area and in different local transport areas, international services, 1+ outbound services and inbound toll-free services. PAETEC also offers ancillary long distance services, such as audio and web conferencing services. In those instances in which PAETEC is not able to connect a customer to its network, the company resells the long distance services of other communications carriers. PAETEC generally sells its long distance services as part of a bundle that includes one or more of its local services offerings, its other network services offerings and/or its integrated solutions offerings.

Access Services. In addition to services it provides to its retail end-user customers, PAETEC offers switched and dedicated access services that other communications providers use when they originate or terminate long distance calls to or from PAETEC s retail end-user customers. PAETEC also provides access services to other local exchange carriers when it terminates local calls made by the customers of other local carriers.

Related Services. PAETEC offers its customers in some regions the following additional services that relate to its core business:

IP traffic classification. PAETEC s service management tools enable customers to classify their IP traffic into tiers for voice, video conferencing, enterprise data and Internet traffic. These tools permit some types of traffic to be prioritized to ensure higher quality during transmission and delivery.

Network storage. PAETEC s VPN services provide the company s customers with the ability to store and share files on network-based storage devices. Customers can access their files remotely or via their VPN connection and establish unique privileges on all shared files.

PC back-up. PAETEC provides its virtual private network customers with the application-based ability to back up their workstations to PAETEC s network-based storage devices, as well as to restore backed-up files that otherwise might be lost or damaged.

Table of Contents

Virtual NXX. PAETEC offers its business customers a remote office feature, known as virtual NXX, that enables them to place from any location calls that appear to be originating from their offices, as well as a simultaneous ring feature that provides customers with the ability to have their calls ring at multiple locations, affording customers greater flexibility than traditional call forwarding.

Carrier Services

PAETEC supplements the network services it provides to end users on a retail basis with its wholesale offering of voice and data carrier services to other communications providers and to larger-scale purchasers of network capacity. PAETEC s carrier services customers include communications companies that resell PAETEC s local and long distance services, interactive voice response providers, VoIP providers, other competitive carriers such as PAETEC, wireless service providers, web services providers and Internet service providers. PAETEC derived approximately 16.2% of its total revenue for 2010 from its carrier services.

PAETEC offers the following services to some or all of its carrier customers:

- dedicated local services, including primary rate interface, or PRI, services, that provide high capacity local service for carrier access services, such as dial-up Internet access and VoIP services;
- local voice and related enabling services, such as digital loop carrier services and local switching services;
- long distance network services;
- origination, including toll-free origination, for competitive local providers and other carriers;
- end-user MPLS aggregation services that provide secure IP communications connections between carrier end users and single or multiple network points of presence, or POPs, of the carrier;
- private line services to allow customers to enhance their network and/or to provide bandwidth to their end users;
- local access to Internet service providers;
- high-speed Internet connectivity for Internet service providers and web services applications;
- Internet transit services that provide global routing;
- physical fiber circuitry without electronics, sometimes referred to as dark fiber, enabling the customer to light, or activate, fiber circuitry for purposes of providing bandwidth services to their end users; and
- collocation services in which the customer s equipment is installed in PAETEC s network equipment centers.

The majority of PAETEC s carrier services revenue is generated from terminating and originating communications traffic to and from end-user customers on the PAETEC network that is sent to and from these end users by other communications companies. PAETEC historically has generated the majority of these revenues by terminating and originating traditional long distance services. Through its centralized network equipment centers, PAETEC provides its regional customers with the flexibility to extend their coverage areas without extending their operational centers or investing in additional personnel.

Integrated Solutions

PAETEC also offers a variety of customized services that help network and carrier services customers build and operate their own data and voice networks. Sales of these offerings can follow or often result in subsequent sales of one or more of PAETEC s network or carrier services. These customized services enhance customer retention and frequently represent a decisive factor for customers that choose PAETEC over its competitors for the provision of network services. PAETEC derived approximately 7.1% of its total revenue for 2010 from its integrated solutions.

Table of Contents

Data Center Solutions. PAETEC operates seven data centers in the United States, four of which were deployed during 2010 or early 2011 and one of which was acquired as part of the Cavalier transaction. At each of these facilities, PAETEC provides a highly secure, protected and environmentally controlled location for PAETEC s customers to maintain their critical data, server operating applications and network and communications assets. These data centers, which are accessible 24 hours a day, seven days a week, also are utilized by PAETEC to provide managed cloud computing and virtual services, such as virtual hosting and data storage, to PAETEC customers.

Applications Services. PAETEC s Pinnacle software product provides customers with many of the network management and cost allocation capabilities of a telecommunications carrier. Customers using PAETEC s software are able to perform rate inquiries, initiate trouble ticketing, track work orders and perform other tasks associated with maintaining a large scale internal telecommunications network. In addition, Pinnacle software customers can track and allocate the costs of voice, data and other communications charges at the individual, departmental and general ledger levels. Customers can license the software or utilize the functionality through a managed solution hosted by PAETEC in one of its data centers. PAETEC s target market segment for the Pinnacle software products includes institutions with large internal telecommunications networks, such as Fortune 1,000 companies, universities and government agencies.

Network Design and Implementation. PAETEC offers design, installation and maintenance services for networks, including local and wide area networks, located on the customers premises.

Energy Services. PAETEC sells electricity to business and residential customers, primarily in certain geographic regions in New York state, as a competitive electricity supplier.

Customer Premise Equipment Sales, Installation and Management Services. PAETEC sells and installs equipment located on its customers premises. This equipment, including products from Avaya and Cisco, historically has included private branch exchanges, local area networks and servers and routers. Through its Allworx Corp. subsidiary, PAETEC develops and sells complete phone and network systems and provides software and digital hardware engineering services specifically designed to benefit small and medium-sized businesses. In addition, to complement its own work force, PAETEC establishes relationships with local equipment installation companies to sell and install equipment that PAETEC does not sell directly.

PAETEC s Network Architecture and Deployment

Overview. PAETEC has developed, installed and continues to invest in a flexible network that facilitates delivery of its data and voice services. To deploy its network, PAETEC employs:

- a facilities-based network pursuant to which PAETEC owns approximately 36,700 route miles of fiber in portions of 39 states and the District of Columbia; and

- a cost-effective strategy of combining telephone and data transmission lines that it leases with other electronic network components that it owns and operates.

This network deployment strategy has allowed PAETEC to enter new markets relatively rapidly and to offer its customers flexible technological solutions tailored to their specific needs. PAETEC believes that this network deployment strategy also will facilitate the company s adoption and delivery of new technologies.

Last Mile Connections. PAETEC connects its customers to its network by leasing special access digital T1 transmission lines, unbundled network element, or UNE, high capacity loops, which we refer to as UNE digital T1, as well as mid-bandwidth (3-20Mb) and high-bandwidth (20Mb+) Ethernet access links. All of these types of access lines provide a dedicated connection between customer locations and PAETEC switches. PAETEC has obtained the majority of these leased digital transmission lines from the major incumbent local exchange carriers such as AT&T Inc., Verizon Communications Inc., Qwest Corporation and CenturyLink,

Inc. PAETEC also has relationships with providers to supply alternative types of last mile connectivity to certain locations. PAETEC s strategy traditionally has been to improve reliability through alternative network paths by forming relationships with multiple providers of last mile access to locations where alternative last mile facilities are available, as well as to lower its costs through competitive procurement. PAETEC is able to provide direct access to a limited number of buildings using its own last mile facilities. The PAETEC-owned facilities are capable of providing up to 1Gigabit of Ethernet managed services to the customers located in those buildings, as well as services via digital system cross-connect frame, or DSX, and very high capacity optical carrier, or OC-n, lines. In certain geographic areas, PAETEC also can provide direct wireless last mile access using a variety of speeds over wireless spectrum at the DSX, OC-n, or Ethernet levels of 10, 100 or 1,000 megabits per second.

Packet Technology. PAETEC s network infrastructure and operations support systems enable it to control the types of services that it offers, how these services are packaged and how they are integrated to serve customers. Through its installation of IP routers at its switch sites, PAETEC has broadly deployed packet-based technology across its service area as it migrates from traditional circuit-switching technology. Circuit switch-based systems, which historically have dominated the public telephone network, establish a dedicated channel for each communication, such as a telephone call for voice or fax, maintain the channel for the duration of the call, and disconnect the channel at the conclusion of the call. Packet-switched systems format the information to be transmitted into a series of shorter digital messages called packets. Each packet consists of a portion of the complete message plus the addressing information to identify the destination and return address. Unlike circuit-switching, packet-switching does not require a single dedicated channel between communication points. This type of communication between sender and receiver is considered connectionless, rather than circuit -based. Traffic over the Internet, which is a connectionless network, uses packet-switching technology. We believe a transition to combining the delivery of PAETEC data and voice services over a converged packet-based network enables us to streamline the delivery of core communications services to our customer base in a more flexible manner than circuit-switching technology has permitted, to deliver a new generation of product offerings, and to leverage our network assets more effectively and efficiently.

Network Infrastructure and Backbone Network. PAETEC s network backbone enables it to offer high-quality broadband Internet access and VPN services. This backbone consists of high-capacity fiber optic facilities that allow PAETEC to transport traffic between points on its network in portions of 39 states and the District of Columbia. As of March 31, 2011, PAETEC s fiber backbone network spanned approximately 26,100 intercity and 10,600 metropolitan local route miles and encompassed approximately 1,577,000 intercity backbone fiber miles and 743,000 fiber miles of metropolitan local fiber optic cable. PAETEC primarily leases these facilities between locations where it does not operate its fiber network. The packet-switching portion of PAETEC s backbone is based on Internet Protocol, which is a broadly deployed standards-based protocol that allows unrelated computer networks to exchange data and is the technological basis of the Internet. IP technology has enabled PAETEC to accelerate network traffic flow and has made it easier and less costly for PAETEC to manage its network. This technology generally makes more of the network capacity available for revenue-generating customer traffic. PAETEC s infrastructure is intended to provide a network switching presence closer to the customer to reduce access mileage and switching costs, and to allow the company to expand its network rapidly to meet customer demand. The regional design also is intended to enhance service reliability and allow PAETEC to improve quality and performance.

Collocations. As of March 31, 2011, PAETEC had approximately 1,100 collocations, enabling it to access lower-cost special access digital T1 lines and UNE digital T1 lines from within the central offices of regional Bell operating companies, or RBOCs, to connect to customer locations in local service areas using shorter access loops. In addition, PAETEC can serve outlying areas of its markets where it does not have collocations by using enhanced extended loops, or EELs, or special access T1 lines to connect more remote customer locations to its network.

Table of Contents

Geographic Markets

As of March 31, 2011, PAETEC provided service in 86 of the top 100 metropolitan statistical areas and operated 166 switches.

Sales and Marketing

Network Services Sales Strategy. PAETEC targets business customers that it believes can benefit from the company s value-added services. PAETEC pursues a decentralized sales strategy, which affords its sales representatives substantial flexibility to negotiate the pricing and other terms of its customer agreements for medium-sized and large businesses, subject to meeting specified revenue and profitability requirements. For this strategy to succeed, PAETEC must be able to attract, train, motivate and retain skilled sales professionals. PAETEC seeks to recruit sales representatives with experience working for other communications providers, telecommunications equipment manufacturers and network systems integrators in the company s existing and target markets. PAETEC then augments that experience with an internal training program and software tools that provide its sales representatives with the information they need to negotiate profitable customer contracts.

Sales of network services in each of the markets in which PAETEC provides such services to medium-sized and large businesses is led by PAETEC s President of National Sales and Service, who is responsible for the acquisition and retention of all network services accounts and who reports directly to PAETEC s Chief Executive Officer. Network sales teams are divided into four geographic regions, with a regional sales president responsible for managing all direct sales, agent sales, account development, network design and service engineering in the assigned region. Each sales team generally includes branch sales managers, account managers, sales representatives, sales engineers and field technicians. PAETEC s sales teams use a variety of methods to qualify leads and schedule initial appointments, including developing relationships with local industry associations and obtaining customer referrals. PAETEC believes this regionalized sales structure allows the company to maintain personalized customer service across its national operations.

PAETEC s sales representatives generally make the initial customer contacts and sales. After the initial sale, PAETEC provides follow-up support and the sale of additional services, based on the size of the customer account, either through an account manager assigned to the customer or as part of the customer service organization. PAETEC also provides the local sales offices with technical resources to support the sales force and to coordinate switching the customer to PAETEC service. PAETEC s service agreements with new customers generally have a fixed period initial term (averaging approximately 36 months as of March 31, 2011) and a specified volume commitment, which is typically measured on a monthly basis. The service agreement may be terminated by the customer at any time following a specified notice period and upon payment of a termination fee. Following expiration of the initial term, PAETEC seeks to enter into a new term agreement with the customer. If a new agreement is not reached, the initial agreement will continue either on a term or monthly basis. Some of PAETEC s integrated solutions agreements have initial terms of up to five years.

PAETEC s network services sales force uses proprietary software tools to allow the sales force to create a customized solution for each prospective customer and to conduct profitability and pricing analysis for use in preparing proposals. This procedure serves to ensure that PAETEC maintains its focus on obtaining customers that meet internal profitability standards, while illustrating the potential benefits that a customer may realize by using a broader bundle of services. The focus of the software tool is to afford PAETEC s network services sales representatives maximum flexibility in pricing individual services so long as each bundled sale is profitable. In addition, through its Equipment for Services program, PAETEC offers flexible options for the customer to finance its purchases of hardware and software by including those charges on the network bill. Thus, PAETEC s sales representatives can customize their sales approach to the unique requirements, budgetary constraints, and price sensitivities of each customer. PAETEC believes that this pricing flexibility provides its sales force with a competitive advantage over the sales efforts of many other telecommunications carriers and allows the company to position itself as a flexible and responsive service provider at the initial point of contact with customers.

Network Services Sales Force. As of March 31, 2011, over 1,300 of PAETEC s employees were dedicated to developing and supporting its direct sales and marketing activities. As of the same date, PAETEC maintained a total of 92 sales offices in 36 states and the District of Columbia. Each sales office is generally staffed with at least one sales manager, who has primary responsibility for the results of that office. PAETEC uses its sales offices not only to target businesses and other customers operating within its markets, but also to solicit and service national accounts. To increase operating efficiency, some of its sales offices support the sales teams for multiple markets.

PAETEC requires each new member of its direct sales force to participate in an initial in-house training program, which includes seminars, on-the-job training and direct one-on-one supervision by experienced sales personnel. PAETEC also requires members of its direct sales force to participate in an ongoing training program designed to enhance their knowledge of the communications industry, the company s services and the needs of its targeted customers. PAETEC seeks to motivate its direct sales force with a total compensation program that includes base salary, a cash commissions plan, and eligibility to participate in PAETEC s long-term equity plan. The PAETEC sales commission program is primarily designed to reward the addition of new profitable customers and the sale of additional products and services to existing customers. The commission program also includes an element for some sales personnel that is designed to promote account retention and minimize customer turnover.

The efforts of PAETEC s direct sales force are complemented by marketing activities conducted by independent sales agents. PAETEC seeks to select sales agencies that are well known to medium-sized and large businesses and institutions in their markets, and trains its sales agents on how to retain and develop the customer accounts they introduce to the company. For 2010, customers referred to PAETEC by its sales agents generated approximately 33.7% of the company s network services revenue. As of March 31, 2011, approximately 140 of its employees were dedicated to developing and supporting its agent program.

In early 2011, PAETEC established sales divisions separate from its regional sales structure to sell and market services to small business and residential customers as well as to sell and market to national accounts.

Carrier Services Sales Strategy. Carrier services sales in each of the markets in which PAETEC provides such services are led by PAETEC s Senior Vice President of Wholesale Services, who is responsible for the acquisition and retention of all carrier services accounts and who reports directly to PAETEC s Chief Executive Officer. Initial sales are made through national account managers located in various sales offices throughout the company s markets. Sales support is provided through carrier sales account managers and sales engineers. As of March 31, 2011, approximately 60 of PAETEC s employees were dedicated to developing and supporting its carrier sales organization.

Customer Service. PAETEC believes that customer service is a critical element in attracting and retaining customers in the communications industry. PAETEC has designed its customer service strategy to allow it to meet its customer needs rapidly and efficiently. PAETEC operates customer service centers in Cedar Rapids, Iowa, Rochester, New York and Palm Harbor, Florida and also outsources some support functions with respect to residential and small business customers to a third-party service provider. Functions handled by the customer service operations include billing questions, order inquiries and changes to services. PAETEC operates network operations centers, or NOCs, in Rochester, New York, Charlotte, North Carolina and Richmond, Virginia. PAETEC operates a NOC with a network health center in Cedar Rapids, Iowa. The functions handled by the NOC portion of the Cedar Rapids facility will be transferred to the Rochester network operations center before the end of 2011. The network health center, which is responsible for monitoring the nationwide PAETEC network 24 hours a day, seven days a week, will remain in Cedar Rapids. The NOCs and the network health center are staffed by skilled technicians who complete a certification program to advance through four levels of proficiency. The network operations center staff evaluates any out-of-service or service affecting condition and directs remedial action to be implemented by PAETEC s technical personnel or, where appropriate, its equipment vendors or external service providers. In addition, the network operations center staff maintains contact with the customer and prepares reports documenting the service issue and any corrective action taken.

Table of Contents

Marketing. In its markets, PAETEC seeks to position the company as the high-quality alternative for communications services by offering network reliability, increased customer support and a broad spectrum of communications services at competitive prices. PAETEC intends to continue to build its reputation and brand identity by working closely with its customers to develop services tailored to the customer s particular needs. PAETEC implements targeted promotional efforts that emphasize the breadth of its communications solutions and its ability to deliver a cost-effective integrated services package to its target customer base.

Customer Concentration. No single customer, or group of related customers, represented 10% or more of our total operating revenues for 2010, 2009 or 2008.

Back Office Systems

PAETEC believes that its information systems and procedures for operations support and other back office systems enable it to price its services competitively, to meet the needs of its customers and to interface with other carriers. PAETEC utilizes Oracle Metasolv Software as its primary operational support system and also uses the RevChain billing platform. PAETEC is continuing its integration efforts to consolidate the operational support systems and the billing systems of acquired companies, including Cavalier, with those for PAETEC.

PAETEC has developed a common sales tool that uses a combination of Oracle s E-business suite and customized internal software. All network services sales personnel submit prospects and sales forecasts as well as generate customer proposals and contracts through this system. This sales tool enables PAETEC to have real-time, single source data on sales performance across the country. PAETEC completed its consolidated customer portal, PAETEC Online, in 2010, and continues to implement numerous customer self-service functions available via the Internet.

Acquisitions

To supplement its internal growth, PAETEC has pursued a targeted acquisition strategy that has sought acquisition candidates that fulfill one or more of the following objectives:

- to increase its penetration of PAETEC s existing markets;
- to expand into new markets;
- to augment the geographic scope of PAETEC s network fiber-based assets, primarily in high density markets; and
- to enhance PAETEC s ability to sell and deliver value-added services.

PAETEC continues to seek acquisition candidates that will add customers and cash flow to its existing network services business or that will enhance its operating efficiencies by lowering access costs through the acquisition of fiber-based assets. In accordance with this strategy, PAETEC focuses its acquisition efforts on other competitive carriers, local and long distance providers, enhanced service providers, network integrators and equipment solutions providers. From time to time, PAETEC may consider selective acquisitions of the types of businesses that PAETEC believes will enhance its package of service offerings, increase its customer base and bring experienced back office, technical and customer service personnel to the company.

Subsidiary Reorganization

Following a comprehensive review of its organizational structure, PAETEC completed in March 2010 a reorganization involving some of PAETEC Holding Corp. s direct and indirect wholly-owned subsidiaries that was designed to achieve various administrative and tax efficiencies. As of December 31, 2010, all but two of PAETEC Holding Corp. s subsidiaries are wholly owned, directly or indirectly, by PAETEC Corp., which in turn is a direct, wholly-owned subsidiary of PAETEC Holding Corp.

Competition

The telecommunications industry is highly competitive. PAETEC competes primarily on the basis of a flexible product solution, the availability, reliability, variety, price and quality of its service offerings, and the quality of its customer service. PAETEC s competitors in the provision of local and long distance, Internet connectivity, and related network services include:

- incumbent carriers such as AT&T, Qwest, Verizon and CenturyLink;
- local and long distance resellers, and other competitive carriers like PAETEC; and
- other types of companies, including cable companies, Internet service providers, wireless carriers, satellite carriers, equipment vendors, network integration outsourcing vendors, and businesses offering long distance data and voice services using VoIP.

Incumbent Carriers. PAETEC believes that its primary competition in each of its markets will continue to be the incumbent carriers, which are the large telephone companies, such as AT&T, Qwest and Verizon, that historically provided local telephone service before the enactment of Telecommunications Act of 1996. Today, these companies offer a comprehensive package of local, long distance and Internet services to their customers in direct competition with PAETEC. AT&T and Verizon, which also have wireless affiliates, are investing to upgrade their networks, which will enhance their ability to offer a range of services and compete with PAETEC.

Incumbent carriers generally have long-standing relationships with their customers, have resources substantially greater than PAETEC s and have the potential to subsidize competitive services with revenue from a variety of other businesses. The mergers between AT&T and SBC Communications, Inc., between Verizon and MCI, Inc., and between AT&T and BellSouth Corporation, as well as the proposed merger between CenturyLink and Qwest provide these carriers with significant operating efficiencies and substantial marketing, financial and technical resources. The Communications Act of 1934, as amended, which we refer to as the Communications Act, and past decisions by the Federal Communications Commission and state regulatory commissions have imposed extensive obligations on the incumbent carriers to allow non-incumbent carriers such as PAETEC to interconnect with the facilities of the incumbent carriers and to obtain critical network elements, such as digital T1 transmission lines, from those carriers. The scope of such obligations, however, has been narrowed by court decisions and regulatory changes. These developments, which have resulted in increased pricing flexibility and relaxed regulatory oversight for incumbent carriers, may have a negative impact on PAETEC s business opportunities and competitive position.

FCC decisions and policy initiatives have provided incumbent carriers with increased pricing flexibility for their private line, special access and switched access services. These FCC decisions and initiatives provide that, when an incumbent carrier demonstrates that competitors have made specified competitive inroads in providing a specified federally-regulated service in a geographic area, the incumbent carrier in that area may offer discounts to large customers through contract tariffs, engage in aggressive volume and term discount pricing practices for its customers, or otherwise free itself of regulatory constraints. Legislatures and regulatory authorities in some states have adopted or are considering similar forms of deregulation. These actions could have a material adverse effect on the ability of competitive carriers, including PAETEC, to compete with the incumbent carriers.

Other Competitors. Other current and prospective competitors in the local and long distance voice and data markets include the following:

- cable television companies;
- Internet service providers;
- VoIP providers;

wireless carriers; and

others, such as resellers of local and long distance telephone services, microwave carriers, service providers offering alternative access methods, and private networks built by large end users.

Table of Contents

Cable Television Companies

Cable television companies such as Cablevision Systems Corp., Comcast Corporation, Cox Communications Inc. and Time Warner Cable Inc. have continued to deploy telecommunications and broadband Internet access services aggressively to customers on a broad scale to primarily residential and small business customers. These companies initially deployed telecommunications services using circuit-switched facilities, but, increasingly, they are using VoIP applications and other technologies to provide voice services in a less costly, more efficient manner. In addition, some of these companies resell wireless services, which potentially could lead to the creation of new bundled competitive service offerings that incorporate multimedia components of cable television and wireless broadband Internet access services at competitive rates. Some of these companies have acquired a financial interest in spectrum capable of accommodating advanced mobile wireless services, which could result in additional competitive offerings.

Internet Service Providers

Advances in digital transmission technologies have created opportunities for the transmission of voice and data services over the Internet. Broadband Internet service providers such as AT&T, Qwest, Verizon and the largest cable television companies are exploiting their market position as incumbent providers of telecommunications or cable television services to promote their broadband Internet services and related voice and data applications. If successful, these plans will increase the number of competitive providers of broadband service, which could place additional downward pressure on prices for this service.

VoIP Providers

PAETEC expects to face increasing competition from companies offering long distance data and voice services using VoIP. The emergence of these companies could present a competitive threat, principally because the regulatory classification of VoIP remains unclear. Providers of VoIP services may be able to avoid significant costs, such as the payment of switched access intercarrier compensation fees, if these regulatory classification issues are resolved in favor of VoIP providers. Such a resolution could impede PAETEC s ability to compete against these providers on the basis of price.

Wireless Service Providers

National carriers such as AT&T Mobility, Sprint Nextel Corporation, T-Mobile USA, Inc. and Verizon Wireless, as well as smaller regional companies, provide voice services that increasingly are viewed by consumers as competitive with wireline telecommunications offerings. Robust growth in wireless usage has caused a decline in the volume of voice traffic carried by PAETEC and other wireline carriers. Cable television companies and other companies have entered into arrangements to resell or re-brand wireless services. Technological advances have allowed wireless service providers to add data transmission, Internet access services and next-generation services, such as mobile multimedia products. Recent spectrum auctions and other regulatory changes have afforded wireless service providers access to substantial additional spectrum resources that can be used for deployment of high-speed broadband wireless services. New wireless service providers could include Microsoft Corporation and Google Inc. using unlicensed white space spectrum, which is unused wireless spectrum between broadcast television channels. Additional spectrum auctions in the next few years may accelerate the deployment of wireless high-speed broadband networks and offerings. In addition, the introduction of fixed wireless applications has facilitated the creation of companies that are in the process of installing equipment and building networks that may offer the same types of services that PAETEC offers or intends to offer. A commercially successful deployment of WiMax technology, for example, would facilitate the development of similar broadband access services on a fixed and mobile basis. Some wireless service providers have long-standing relationships with customers and financial, technical, marketing and other resources substantially greater than PAETEC s relationships and resources.

In the last few years, consolidation within the wireless industry has resulted in significant growth for the largest wireless providers. Wireless Holdings, Inc. and Sprint Nextel, together with a group of cable television operators and information technology companies, recently made major investments in Clearwire Corp. Continued consolidation within the wireless industry could further enhance the economies of scale that would improve the competitiveness of wireless service providers in the telecommunications market.

PAETEC expects that new competitors, including large computer hardware, software, media and other technology and telecommunications companies, will enter the tailored, value-added network services market, resulting in even greater competition. Some telecommunications companies and online services providers are currently offering broadband Internet access services, or have announced plans to expand these services and other network services. Other companies, including Time Warner, also have obtained or expanded their broadband Internet access products and services as a result of acquisitions. Still others, such as Google, are developing new technologies and applications, the effect of which PAETEC cannot determine at this time. These developments may permit PAETEC s competitors to devote greater resources to the marketing of existing competitive products and services and the creation of new competitive products and services. In addition, the ability of some of PAETEC s competitors to bundle other services and products with outsourced corporate networking services or Internet access services could place it at a competitive disadvantage.

Industry Consolidation. Consolidation of telecommunications providers has occurred with relative frequency over recent years and is expected to continue to create larger, better situated competitors that may put PAETEC at a greater competitive disadvantage. For example, the mergers between AT&T and SBC, between MCI and Verizon, and between AT&T and BellSouth increased the strength of those combined companies in the local, long distance, data and wireless markets. These mergers also decreased the competitive alternatives available to PAETEC for various network elements and services. The proposed merger of CenturyLink and Qwest will create an incumbent local exchange carrier, or ILEC, with a presence in 35 states. Many other incumbent and non-incumbent carriers also are expanding their facilities-based and non-facilities-based offerings in the long distance and data markets. Other competitive carriers already have established full service local operations in some of PAETEC s current and target markets. Many competitive carriers and independent long distance service providers have been struggling financially, but PAETEC cannot accurately predict which of these carriers will be able to compete effectively against it over time. Recent consolidation activities involving telecommunications providers also have begun to blur the line between different types of competitors in a manner that may also make it more difficult for PAETEC to compete. In February 2010, Windstream Corporation, a mid-sized incumbent local exchange carrier, acquired NuVox, Inc., a competitive local carrier that has competed with PAETEC in a variety of markets in the Southeast. In January 2011, the FCC granted approval of the assignment and transfer of control of broadcast, satellite, and other radio licenses from General Electric Company to Comcast Corporation, which allows GE and Comcast to create a joint venture involving

NBC Universal, Inc. and some Comcast properties. PAETEC cannot accurately predict all of the changes that the marketplace for telecommunications services may continue to experience as a result of this consolidation trend.

Regulation

PAETEC s services are subject to varying degrees of federal, state and local regulation. The following summary of regulatory developments and legislation does not purport to describe all current and proposed federal, state and local regulations, administrative rulemakings and legislation affecting PAETEC. Federal and state legislation and regulations governing telecommunications and related services are the subject of ongoing judicial proceedings, rulemakings and legislative initiatives that could change, in varying degrees, the manner in which the communications industry operates.

Under the Communications Act, the rules of the FCC, and comparable state laws and regulations, PAETEC and other competitive carriers are required to provide service upon reasonable request and to interconnect their networks with the networks of other carriers, and are subject to other regulatory obligations, some of which are described below. The FCC exercises jurisdiction over PAETEC s facilities and services to the extent that they are used to provide, originate or terminate interstate or international communications services offered to the public. State regulatory commissions regulate the same facilities and services to the extent they are used to originate or

Table of Contents

terminate intrastate communications services offered to the public. In addition, as a result of the passage of the Telecommunications Act of 1996, state and federal regulators share responsibility for implementing and enforcing rules to allow new companies to compete with the local phone companies that historically have operated as monopolies.

Existing federal and state regulations are subject to amendment by federal and state administrative agencies, judicial proceedings, and legislative action that could affect, in varying degrees, the manner in which PAETEC operates. Bills intended to amend the Communications Act are introduced in Congress from time to time and their effect on PAETEC and the communications industry cannot always be predicted. Proposed legislation, if enacted, could have a significant effect on PAETEC s business, particularly if the legislation impairs PAETEC s ability to interconnect with incumbent carrier networks, lease portions of other carriers networks or resell their services at reasonable prices, or lease elements of networks of the incumbent local exchange carriers under acceptable rates, terms and conditions. PAETEC cannot predict the outcome of any ongoing legislative initiatives or administrative or judicial proceedings or their potential impact upon the communications and information technology industries generally or upon PAETEC specifically.

Federal Regulation

PAETEC is regulated by the FCC as a non-dominant carrier subject to minimal regulation under the Communications Act. Both the Communications Act and the FCC s rules and policies implementing the Act generally favor entry into local and other telecommunications markets by new competitors, such as PAETEC, and seek to prevent anti-competitive practices by incumbent carriers.

Licenses and Authorizations. The FCC requires all telecommunications service providers, including non-dominant carriers such as PAETEC, to maintain authorizations to provide or resell domestic long distance and international services. The FCC generally has the power to modify or terminate a carrier s authority to provide domestic long distance or international services for failure to comply with federal laws or FCC regulations and may impose fines or other penalties for violations. In addition, the FCC maintains jurisdiction to act upon complaints filed against any telecommunications service provider for failure to comply with statutory or regulatory obligations.

Tariffs and Retail Pricing Requirements. Under the Communications Act, PAETEC is subject to the general requirement that its charges, practices and classifications for communications services must be just and reasonable, and that it refrain from engaging in any unjust or unreasonable discrimination with respect to its charges, practices or classifications. The FCC must grant its approval before any change in control of any carrier providing interstate or international services, or of any entity controlling such a carrier, and before the assignment of any authorizations held by such a carrier.

Measures Designed to Speed Competitive Entry. The Communications Act imposes a variety of duties on local telephone service providers, including PAETEC, to promote competition in the provision of local telephone services. These duties include requirements to:

- interconnect directly or indirectly with other carriers;
- permit resale of services;
- permit users to retain their telephone numbers when changing carriers;
- provide competing carriers access to poles, ducts, conduits and rights-of-way at regulated prices; and
- establish reciprocal compensation arrangements for the transport and termination of telecommunications.

Table of Contents

Incumbent carriers also are subject to additional duties that facilitate local market entry by competitive carriers such as PAETEC. For example, incumbent carriers must:

- permit competitors to collocate their equipment on the premises of the incumbent carriers at cost-based rates and on a nondiscriminatory basis;
- allow competitors to make use of designated elements of incumbent carrier networks on an unbundled basis, and on non-discriminatory, cost-based rates, in combination with or separate from other wholesale or special access services purchased from the incumbent; and
- offer wholesale versions of their retail telecommunications services for resale at discounted rates.

Interconnection Agreements. Incumbent carriers are required to negotiate statewide interconnection agreements in good faith with competitive carriers such as PAETEC that set forth the terms for, among other items, interconnection, collocation, intercarrier compensation, access to unbundled network elements and reselling of an incumbent carrier s services. If the negotiating carriers cannot reach agreement within a prescribed time, either carrier may request binding arbitration of the disputed issues by a state regulatory commission. In addition, carriers are permitted to adopt or opt-in in their entirety an existing state commission-approved interconnection agreement between an incumbent carrier and another carrier in the same state. PAETEC has interconnection agreements with incumbent carriers in 47 states and the District of Columbia that encompass all local exchange markets in which PAETEC currently offers local services. Each statewide interconnection agreement with an incumbent carrier allows PAETEC to enter other local exchanges served by that same incumbent in that state. Each interconnection agreement and subsequent amendments must be approved by the applicable state regulatory agency before becoming effective. Although parties may negotiate prices contained in the interconnection agreement, such statewide agreements typically incorporate prices for interconnection, collocation, intercarrier compensation and UNEs that have been established by the state regulatory agency in generic proceedings for the incumbent carrier using the FCC s approved pricing methodology. When an interconnection agreement does not resolve a particular operational issue, PAETEC and the incumbent carrier seek resolution of those issues through informal and formal dispute processes, including commercial negotiations or arbitration.

Interconnection agreements typically have terms of three years, although the parties may mutually agree to extend or amend such agreements. If PAETEC cannot negotiate new interconnection agreements or renew its existing interconnection agreements in each state on acceptable terms, or find an acceptable interconnection agreement available for opt-in, PAETEC may invoke its ability to seek binding arbitration before state regulatory agencies. The arbitration process conducted on a state-by-state basis can be costly and time-consuming, and the results of arbitration may be unfavorable to PAETEC. If PAETEC is not able to renegotiate or enter into interconnection agreements on acceptable terms, or if it is subject to unfavorable arbitration decisions, PAETEC s cost of doing business could increase and its ability to compete could be impeded. Moreover, PAETEC s interconnection agreements with companies other than incumbent local exchange carriers (such as wireless and VoIP providers and other competitive carriers) are not subject to the statutory arbitration mechanism, making it potentially more difficult to reach any agreement on terms PAETEC views as acceptable.

The availability of acceptable interconnection agreements that competitive carriers such as PAETEC can opt into without incurring the expense of lengthy negotiation and arbitration with an incumbent carrier in each state has significantly declined due to industry consolidation. It is likely that competitive carriers such as PAETEC will be required to invest more resources than in the past to secure acceptable interconnection agreements, or be willing to accept less favorable terms of interconnection and access to the ILEC s network.

In March 2007, Qwest provided notice to PAETEC that Qwest was terminating all current interconnection agreements with PAETEC s McLeodUSA operating subsidiary. The termination notice began a negotiation period for new interconnection agreements for the 12 Qwest states in which PAETEC interconnects with Qwest on a facilities-basis. However, in January 2011, CenturyLink and Qwest offered a voluntary commitment to secure FCC approval of their proposed merger that would entitle PAETEC to extend any existing interconnection agreement with Qwest for an additional three years after their proposed transaction closes.

Intercarrier Compensation. Interconnected carriers exchange communications traffic, and must establish the compensation arrangements for the use of their respective networks in carrying that traffic for each other. Long distance carriers compensate local exchange carriers for the origination and termination of long distance traffic through the payment of switched or dedicated access charges. Facilities-based telecommunications providers, including wireless carriers, charge other facilities-based telecommunications providers to terminate local traffic on the terminating provider s network. These charges are known as reciprocal compensation. The FCC has established rules governing how much PAETEC may charge for interstate switched access and reciprocal compensation, including rules that apply to traffic bound for Internet service providers. However, the FCC repeatedly has refused to decide whether long distance calls originated in VoIP format are subject to tariffed access charges at the terminating end of the call, resulting in significant confusion and uncertainty within the industry and divergent practices and positions. This uncertainty, combined with the steady growth of VoIP as a percentage of all telecommunications traffic, increases PAETEC s risk on both the revenue and cost sides. Moreover, although the FCC first proposed major reforms to its intercarrier compensation scheme in 2001, it has yet to act on those or subsequent proposals. In February 2011, the FCC issued another notice of proposed rulemaking, or NPRM, that proposes to modify the existing scheme of intercarrier compensation. PAETEC s business could be affected by whether, when, and how the FCC acts to reform its rules in this area.

Universal Service. The FCC has established a federal universal service subsidy regime known as the Universal Service Fund, or USF, which provides subsidies for the provision of telecommunications and information services to rural and other high-cost areas and for discounted communications services to schools and libraries. Providers of interstate telecommunications services such as PAETEC must pay assessments that fund these subsidies. The FCC currently is assessing USF contribution payments based on a percentage of each telecommunications provider s projected interstate and international telecommunications revenue. Carriers are permitted to pass through a specified percentage of their USF contribution assessment to their customers in a manner consistent with FCC billing regulations.

In February 2011, the FCC issued a notice of proposed rulemaking to significantly modify the USF distribution to support universal access to broadband services rather than voice services. The FCC proposal includes limiting the number of carriers eligible to receive funds in a specific geographic area, and asks for comments on a variety of USF-related proposals to support the goal of making broadband access available everywhere in the country. The February 2011 NPRM did not propose changes to the existing USF contribution method, or ask for comments regarding how the contribution formula should be changed to support universal access to broadband services. However, the FCC indicated that a goal of USF reform is to expand the pool of contributors to the USF to enable a reduction in the USF assessment. These and other proposals pending before the FCC related to USF reform are expected to generate considerable debate and their outcome is not predictable. In addition, various states maintain, or are in the process of implementing, their own universal service programs.

Customer Proprietary Network Information. Federal regulations protect the privacy of some subscriber data that telecommunications carriers such as PAETEC acquire in the course of providing their services. This information is referred to as Customer Proprietary Network Information, or CPNI, and includes information related to the quantity, technological configuration, type, destination and amount of use of a communications service. PAETEC must file a verified certification of compliance by March 1 of each year that affirms the existence of training and other sales and marketing processes designed to prevent improper use and unauthorized release of CPNI. A violation of these and related CPNI requirements by PAETEC could subject our company to significant fines or other regulatory penalties.

Network Element Rules. The FCC s current unbundling rules identify some competitive conditions in terms of business line counts and fiber-based collocators at a wire center level that, if such competitive conditions are found to exist, eliminate an RBOC s obligation to offer competitive carriers access to unbundled network elements such as UNE digital T1 or DS3 loops or high capacity transport, as well as combinations of those elements, under federal and state price regulations. Under the current unbundling rules, PAETEC is not able to obtain UNE digital T1 loops at regulated prices from RBOCs in 100 wire centers serving areas.

Table of Contents

Incumbent carriers are permitted to charge just and reasonable rates for network elements in these wire centers and make them available on a deregulated commercial basis. Incumbent carriers also are permitted to designate in the future additional wire centers in which they believe competitive conditions should entitle the RBOC to limit the availability of UNE digital T1 loops, high capacity transport or both, and to make these services available only on a commercial basis.

Pending FCC Proceedings. PAETEC faces substantial uncertainties stemming from ongoing FCC proceedings related to the implementation of the statutory requirements discussed above, as well as ongoing judicial review of various FCC decisions, both of which could result in significant changes to these regulatory obligations. PAETEC cannot predict the outcome of ongoing administrative or judicial proceedings or their potential impact upon the company. The following examples illustrate the types of ongoing rule changes that could affect PAETEC s business:

Special Access Regulatory Regime

PAETEC relies to a considerable extent on special access lines as the last mile facility to reach its customer locations. As a result, the price of special access lines must be available at a rate that allows PAETEC to price its retail offerings to meet its gross margin expectations while remaining competitively priced in the retail market. Incremental increases in prices of special access lines will exert pressure on PAETEC s gross margins. In 2005, the FCC opened an inquiry into whether and how to reform its special access rules. In November 2009, the FCC asked interested parties to respond to several questions regarding the appropriate analytical framework for resolution of issues in its longstanding special access proposed rulemaking proceeding. Interested parties filed initial comments in January 2010 and reply comments were filed in February 2010. In November 2010, the FCC asked companies to voluntarily submit on a confidential basis detailed network data such as fiber maps, lit buildings, collocations, and switch sites. At this time, PAETEC cannot predict when the FCC will issue a decision regarding special access prices or how any such decision will affect its business.

TELRIC Proceeding

A proceeding was initiated at the FCC in 2003 to examine the current rules governing the methodology by which state regulatory authorities set wholesale prices for UNEs, including UNE digital T1 loops, and for collocation, interconnection and intercarrier compensation provided by incumbent carriers to competitive carriers. If the FCC adopts significant changes to the pricing

methodology, incumbent carriers could seek approval from state regulatory commissions to increase their prices for a variety of wholesale services required by PAETEC to provide service to its customers. Such an event could raise the cost of doing business for competitive carriers such as PAETEC. We cannot predict whether the FCC will change its pricing rules, or, if it does so, the extent to which state regulatory commissions will permit incumbent carriers to increase their UNE prices.

Qwest and Verizon Dominant Carrier Forbearance Proceedings

Under the Telecommunications Act of 1996, the RBOCs can petition the FCC to forbear from applying regulations implementing the Act. All of the RBOCs have used the provision to secure deregulation of certain services. Qwest and Verizon have petitioned the FCC on multiple occasions to have the FCC forbear from enforcing the unbundling rules in various markets. In June 2010, the FCC denied the second Qwest petition for forbearance in Phoenix filed in March 2009. In rejecting the Qwest petition, the FCC used a market power test, under which the FCC separately analyzed Qwest s market power in different market segments, such as residential retail, enterprise retail and wholesale. Qwest appealed the denial to a federal appellate court, where the matter remains pending. If the court overturns the FCC s use of a market power test, or remands the denial of forbearance back to the FCC for further consideration, or the FCC upholds or grants any forbearance or similar petitions filed by incumbent carriers in the future affecting markets in which PAETEC operates, PAETEC s ability to purchase wholesale network services from these carriers at cost-based prices that would allow PAETEC to achieve its target profit margins in those markets could be materially adversely affected. The grant of these petitions also would enable incumbent carriers to compete with their competitors, including PAETEC, more aggressively on price in the affected markets.

Intercarrier Compensation

In February 2011, the FCC issued an NPRM to materially modify the compensation arrangements between all carriers for the use of their respective networks. The FCC first initiated a proceeding to reform intercarrier compensation in 2001, and the new NPRM is the fourth issued by the FCC on this subject. The proposed changes, if adopted, would significantly alter the manner in which carriers, including carriers that use different service platforms such as wireless, cable and VoIP, are compensated for the origination and termination of communications traffic and the rates local exchange carriers charge for these access services. The proceeding also will alter the manner in which facilities-based local carriers charge other carriers, such as VoIP providers and wireless providers, for the origination and termination of local communications traffic.

If intercarrier compensation and Universal Service Fund reforms are adopted by the FCC, these reforms could have a substantial effect on PAETEC s access revenues, network capital expenditures and costs of sales.

Broadband Network Management and Net Neutrality Policies. In August 2005, the FCC adopted a policy statement that outlined four principles intended to preserve and promote the open and interconnected nature of the public Internet. The FCC explained at the time that these net neutrality principles are subject to reasonable network management. In January 2008, the FCC sought comment on petitions filed by a number of parties seeking clarification on what conduct constitutes reasonable network management and whether the practice of degrading certain peer-to-peer network traffic is unreasonable or violates the net neutrality principles. In August 2008, the FCC characterized these net neutrality principles as binding and enforceable and stated that network operators have the burden to prove that their network management techniques are reasonable. In that order, the FCC imposed sanctions on a cable broadband Internet access provider for managing its network by blocking or degrading some Internet transmissions and applications in a way that the FCC found to be unreasonably discriminatory. This FCC decision was overturned by a federal appellate court in April 2010. The court ruled the FCC had deregulated broadband services, and, therefore, lacked jurisdiction to enforce net neutrality principles. The FCC issued an NPRM in which it proposed adoption of rules that would require open Internet access subject to a carrier s reasonable traffic management needs. In December 2010, the FCC adopted a narrowed set of network neutrality regulations focused on protecting end-user rights relying on similar jurisdictional grounds previously rejected by the court of appeals. Several parties, including Verizon, appealed the new rules in January 2011.

Expanding Network Access Options. In November 2009, PAETEC and other competitive carriers asked the FCC to initiate a rulemaking to adopt a regulatory structure governing network elements known as 271 Checklist elements. Under the Telecommunications Act of 1996, Bell operating companies are required to make some network elements, such as access loops, transport and local switching, available to competitive local exchange companies at just and reasonable prices in exchange for regaining the ability to offer long distance and information services in their respective local exchange markets, which the RBOCs had been prohibited from offering in their respective local exchanges since 1984. Beginning in 2005, multiple federal appellate courts have determined that state utility agencies do not have authority to regulate the 271 Checklist network element pricing, and that only the FCC has authority to set prices for these network elements. In response to the rulemaking petition, the FCC asked interested parties to comment on the proposed rules. In December 2009, another petition was filed asking the FCC to require RBOCs to provide competitive providers access to bit streams on fiber facilities serving small business locations. The FCC had previously eliminated the RBOC obligation to provide unbundled access to fiber and hybrid loop facilities. Interested parties have filed comments on the proposal. PAETEC cannot predict whether the FCC will proceed with action on either proposal at this time.

[Table of Contents](#)

Other Provisions. Telecommunications carriers such as PAETEC are subject to a variety of miscellaneous regulations that can have cost or operational implications. The regulations, for instance, require the filing of periodic revenue and service quality reports, the provision of services to customers with hearing or speech disabilities and associated funding of telecommunications relay services, the capability to associate a physical address with a calling party s telephone number (E-911), compliance with truth in billing requirements, and cooperation with law enforcement officials engaged in lawful communication intercept or monitoring activities, in addition to regulating telemarketing and slamming, which involves an unauthorized change in a subscriber s carrier of choice. Noncompliance with these and other provisions can result in administrative fines and penalties.

Red Flag Rules. On January 1, 2011, the Federal Trade Commission implemented regulations that require companies that provide services to residential and small business accounts to have defined processes to handle situations that may signal that an unauthorized person could be engaged in fraudulent or identity theft activities. The processes addressing up to 26 red flags must be sanctioned by the company s board of directors. As PAETEC launches new sales in the small business and residential markets, its red flag processes will have to expand to address these protected customer classes.

State Regulation

PAETEC provides local telephone service and other intrastate telecommunications services that are subject to the jurisdiction of state regulatory commissions.

To provide local and intrastate telecommunications services in a state, PAETEC generally is required to obtain a certificate of public convenience and necessity from the state public utility commission and to comply with applicable state regulations, including, in some states, the requirement to file tariffs setting forth the company s terms and conditions for providing services. Certificates of authority can be conditioned, modified, canceled, terminated or revoked by state regulatory authorities for a carrier s failure to comply with state laws or rules, regulations and policies of state regulatory authorities. State utility commissions generally have authority to supervise telecommunications service providers in their states and to enforce state utility laws and regulations. Fines or other penalties also may be imposed for violations. As of March 1, 2011, PAETEC provided local telecommunications services in 46 states and the District of Columbia, and provided intrastate long distance services in 48 states.

State public utility commissions typically require PAETEC to file periodic reports, pay various regulatory fees and assessments, and comply with state regulations governing service quality, billing, consumer protection and other similar issues. State public utility commissions also regulate intercarrier compensation rates between local services providers. Interexchange carriers led by AT&T have urged several state commissions to initiate proceedings to institute generic investigations of switched access rate levels of competitive local exchange carriers such as PAETEC. AT&T, Verizon and Sprint are proposing that state utility agencies should cap such switched access rates at levels charged by RBOCs in the state for the same intrastate access services, or at existing interstate rate levels. AT&T and other interexchange carriers also are pursuing state legislation that seeks to impose caps on intrastate switched access rates charged by competitive carriers such as PAETEC. PAETEC cannot predict the outcome of these state agency investigations into intrastate access rates or legislative initiatives that may arise from time to time. PAETEC s retail rates for enterprise customers are not subject to any price regulation in any of its current or planned markets. Because complying with state regulations can be costly and burdensome, the imposition of new regulations in a particular state may adversely affect the profitability of PAETEC s services in that state.

Some of the states in which PAETEC operates require public utility commission approval before the transfer of a carrier s authority to operate within the state, the transfer of its assets to a new entity, or a change in the control of an entity that controls a carrier operating within the state. Some states also regulate a carrier s issuance of securities, incurrence of debt, guarantees or pledges of security in support of such debt. These requirements

Table of Contents

can delay and increase the cost we incur to complete various financing transactions, including future stock or debt offerings, the sale of part or all of our regulated business, or the acquisition of assets and other entities to be used in our regulated business.

Local Regulation

PAETEC s network is subject to numerous local regulations such as building codes, municipal franchise requirements and licensing. Such regulations vary on a city-by-city and county-by-county basis and can affect the company s provision of both network services and carrier services, as well as, where applicable, video services. In some of the areas where PAETEC provides service, it may be subject to municipal franchise requirements and may be required to pay license or franchise fees based on a percentage of gross revenue or other formula. It is possible that some municipalities that do not currently impose fees could seek to impose fees in the future, and that, following the expiration of existing franchises, they could increase fee levels. In many markets, the traditional local telephone companies do not pay rights-of-way fees or pay fees that are substantially less than those paid by PAETEC. In some markets, PAETEC s McLeodUSA operating subsidiary is objecting to or challenging various fees as improper under state or federal law. The outcome of these challenges cannot be predicted.

Intellectual Property

PAETEC s ability to compete depends in part upon its proprietary rights in its technology and business procedures and systems. PAETEC relies on a combination of contractual restrictions and copyright, trademark and trade secret laws to establish and protect

these proprietary rights. It is the company s policy to require employees, consultants and, if warranted based on the service to be provided, vendors to execute confidentiality agreements upon the commencement of their relationships with PAETEC. These agreements provide that confidential information developed or made known during the course of a relationship with PAETEC must be kept confidential and not disclosed to third parties except in specific circumstances.

The U.S. Patent and Trademark Office has granted PAETEC federal registrations for some of PAETEC s trademarks. Federal registration of trademarks is effective for as long as PAETEC continues to use the trademarks and renew its registrations. PAETEC does not generally register any of its copyrights with the U.S. Copyright Office, but relies on the protection afforded to such copyrights by the U.S. Copyright Act. That law provides protection to authors of original works whether published or unpublished and whether registered or unregistered.

Employees

As of March 31, 2011, PAETEC had approximately 4,500 full-time employees. None of its employees are covered by collective bargaining contracts. PAETEC considers its relationships with its employees to be good.

Properties

PAETEC owns and leases numerous sales offices, switch sites, collocation sites, and other facilities across its nationwide service area. PAETEC s corporate headquarters and one of its network operations centers are located in Fairport, New York. The shared facility consists of approximately 100,000 square feet of office space and is occupied under a 20-year lease expiring in April 2021. In December 2010, PAETEC entered into an agreement with the city of Rochester, New York, under which PAETEC will purchase from the city a parcel of land in downtown Rochester and construct a new headquarters building for an estimated total cost of approximately $54 million. The agreement is subject to numerous conditions, contingencies, and approvals, including the receipt of various forms of governmental financial subsidies. For information about the leased facilities, see Note 12 to the consolidated financial statements appearing elsewhere in this prospectus.

Table of Contents

PAETEC intends to lease additional sales offices and network equipment sites as it expands. PAETEC believes that necessary space will be available on a commercially reasonable basis to accommodate its anticipated growth.

All owned properties secure PAETEC s obligations under its senior secured indebtedness, which as of March 31, 2011 totaled $675 million aggregate principal amount. For information about PAETEC s indebtedness, see Note 6 to PAETEC s audited consolidated financial statements appearing elsewhere in this prospectus.

For additional information about PAETEC s properties, see Business PAETEC s Business PAETEC s Network Architecture and Deployment.

Legal Proceedings

In October 2008, PaeTec Communications, Inc. filed a claim in the Supreme Court for the State of New York, County of Monroe, against Lucent Technologies, Inc., Alcatel USA Marketing, Inc. and Alcatel-Lucent, which we refer to collectively as Alcatel-Lucent, for reimbursement of costs and fees in connection with a patent infringement case brought against PAETEC by Sprint Communications Company L.P., or Sprint, and settled in May 2009. PAETEC s claim against Alcatel-Lucent alleges that because the Sprint claims arose from the use by PAETEC of Alcatel-Lucent equipment, Alcatel-Lucent has an obligation to defend and indemnify PAETEC pursuant to the contract terms under which it sold the equipment to PAETEC. Alcatel-Lucent has denied the claim and counter-claimed against PAETEC for allegedly unpaid switch software licensing charges, and associated late fees. PAETEC believes that it has meritorious defenses against these counter-claims.

From time to time, PAETEC is subject to other legal proceedings in the normal course of its operations. See Business Regulation for information about some of these proceedings.

Table of Contents

MANAGEMENT

Executive Officers and Directors

The table below presents information about our executive officers and directors as of March 1, 2011:

Name	Age	Positions
Arunas A. Chesonis	48	Chairman of the Board, President and Chief Executive Officer
Keith M. Wilson	44	Director and Executive Vice President and Chief Financial Officer, Treasurer
Mario DeRiggi	42	Executive Vice President and President, National Sales and Service
Robert D. Moore, Jr.	42	Executive Vice President and Chief Information Officer
Mary K. O Connell	47	Executive Vice President, General Counsel and Secretary
Algimantas K. Chesonis	45	Senior Vice President, Chief Accounting Officer and Controller
Richard T. Aab	61	Vice Chairman of the Board of Directors
Shelley Diamond	57	Director
H. Russell Frisby	60	Director
Tansukh V. Ganatra	67	Director
Michael C. Mac Donald	57	Director
William R. McDermott	49	Director
Alex Stadler	60	Director
Mark Zupan	51	Director

Our executive officers serve at the pleasure of the board of directors. See Board of Directors Director Qualifications for a discussion of the director qualifications set forth below as part of each director s business history.

Arunas A. Chesonis has served as Chairman of the Board, President and Chief Executive Officer of PAETEC Holding since August 2006. Mr. Chesonis has served as Chairman of the Board, President and Chief Executive Officer of PAETEC Corp., of which he was the founder, since its formation in May 1998 and as Chairman of the Board, President and Chief Executive Officer of its principal operating subsidiary, PaeTec Communications, Inc., since July 1998. Mr. Chesonis was appointed as President of ACC Corp., an international telecommunications company in Rochester, New York, in February 1994 and was elected to its board of directors in October 1994. Mr. Chesonis joined ACC in May 1987 as Vice President of Operations for the U.S. business unit and was named President of ACC Long Distance Corp. in January 1989. Mr. Chesonis also served as President of ACC s Canadian operations and Managing Director of ACC s U.K. enterprise. Before he joined ACC, Mr. Chesonis held several positions within Rochester Telephone Corporation, now known as Frontier Communications Corporation, a subsidiary of Citizens Communications Company.

Director qualifications:

Leadership, industry and operational experience current CEO of PAETEC and former senior executive positions with other telecommunications companies

Keith M. Wilson has served as a director and as Executive Vice President and Chief Financial Officer of PAETEC Holding since August 2006. Mr. Wilson has served as Executive Vice President and Chief Financial Officer of PAETEC Corp. and PaeTec Communications, Inc. since January 2001 and as a director of PAETEC Corp. since March 2006. From June 1999 until January 2001, Mr. Wilson served as Vice President and head of the Telecommunications Finance Group at Union Bank of California, where he focused on sourcing and providing capital for telecommunications services companies in the wireline, wireless and data services markets. From March 1998 until May 1999, Mr. Wilson was a Vice President of Merchant Banking and head of Syndicated Finance for First Dominion Capital, based in New York. Mr. Wilson also held positions with NationsBank from September 1996 until March 1998, Bank of Boston and Fleet Bank.

Director qualifications:

Industry and finance experience current CFO of PAETEC, former head of telecommunications finance group at a bank, and former senior positions with other financial institutions

Mario DeRiggi has served as Executive Vice President and President, National Sales and Service since January 2009. Prior to his current role, he has held positions of increasing responsibility in the areas of sales and account development since joining PAETEC in May 1999 as Vice President and General Manager, including as Senior Vice President, Sales; Executive Vice President, Sales; and President, East Region. In his capacity as Executive Vice President and President, National Sales and Service, Mr. DeRiggi is responsible for managing all of PAETEC s direct sales, agent sales, account development, sales support, and customer service operations. Prior to joining PAETEC, Mr. DeRiggi had over ten years experience in the telecommunications industry, holding positions at Allnet Communications Services, Inc., AT&T, Winstar Communications, Inc. and Cablevision Lightpath, Inc.

Robert D. Moore, Jr. has served as the Executive Vice President and Chief Information Officer of PAETEC Holding since December 2009. Before assuming his current position, Mr. Moore served as the Senior Vice President and Chief Information Officer of PAETEC Holding since February 2007 and in that position with PaeTec Communications since December 2005. Before assuming these positions with PAETEC Holding and PaeTec Communications, Mr. Moore served as Senior Vice President-Information Technology from August 2004 and, beginning in 1998, in various other roles with PaeTec Communications. In his capacity as Senior Vice President and Chief Information Officer, Mr. Moore has been responsible for overseeing operating support systems, systems operations and engineering, and applications development and deployment. Mr. Moore possesses more than 16 years of experience in the telecommunications industry and was employed by ACC Corp. before joining PaeTec Communications.

Mary K. O Connell has served as Executive Vice President, General Counsel and Secretary of PAETEC Holding since January 2011. Ms. O Connell joined PaeTec Communications in September 2001 as Director and Senior Corporate Counsel and held various positions of increasing responsibility prior to her appointment as General Counsel, including service as PAETEC s Corporate Compliance Officer and Vice President and Senior Corporate Counsel. From November 2008 through December 2010, she served as Senior Vice President, General Counsel and Secretary of PAETEC Holding. Before joining PAETEC, Ms. O Connell was in private practice at the law firms of Morrison & Foerster, LLP and Levine, Blaszak, Block & Boothby, LLP in Washington, D.C. and Phillips, Lytle LLP in Rochester, New York. Ms. O Connell s experience before joining PAETEC included work in the areas of commercial law, telecommunications, corporate legal matters, and regulatory affairs.

Algimantas K. Chesonis has served as Senior Vice President, Chief Accounting Officer and Controller of PAETEC Holding since March 2007. Mr. Chesonis has served as Senior Vice President and Controller of PAETEC Corp. and PaeTec Communications since August 2004. Mr. Chesonis served as Vice President of Finance and Controller of PaeTec Communications from July 1998 to August 2004. In his capacity as Senior Vice President and Controller, Mr. Chesonis has been responsible for all aspects of accounting and financial reporting. Mr. Chesonis previously served as Director of Public Reporting for US Foodservice and Audit Manager for the international accounting firm of PriceWaterhouse, LLP. Mr. Chesonis is the brother of Arunas Chesonis.

Richard T. Aab has served as Vice Chairman of the Board of PAETEC Holding, a director position, since February 2007. Mr. Aab co-founded US LEC Corp. in June 1996 and served as its Chairman of the Board from June 1996 to February 2007, when US LEC completed its combination by merger with PAETEC Corp. In 1982, Mr. Aab co-founded ACC Corp. Between 1982 and 1997, he held various positions with ACC, including Chairman of the Board, Chief Executive Officer, President and director. Also during that period, he served as Chairman and director of ACC s international subsidiaries in Canada, ACC TelEnterprises, Ltd., and the United Kingdom, ACC Long Distance UK Ltd. Mr. Aab is a member of the boards of trustees of the University of Rochester, the University of Rochester Medical Center and Rochester Institute of Technology, and is a director

Table of Contents

of several privately-held corporate businesses, including Ovation Payroll, a nationwide payroll processing company, for which he serves as Chairman. From May 2007 to May 2008, Mr. Aab served on the board of directors of Medifast, Inc.

Director qualifications:

Leadership, industry and operational experience former CEO and other senior executive positions with telecommunications companies

Shelley Diamond was appointed to the PAETEC Holding board of directors on March 6, 2009. Ms. Diamond has served since December 2009 as the Global Managing Partner for Young and Rubicam, or Y&R, an advertising agency, where she is responsible for several large, multi-national clients. In this role, she oversees all services rendered by Y&R to these clients around the world. She is also a member of the Y&R board of directors. From July 2007 until December 2009, she served as the Managing Director of the New York office of Y&R, in which role she led the day-to-day operations of the agency, formulating and implementing strategic direction, attracting talent, expanding the office s new media and digital capabilities, and cultivating new business from both existing and new clients. Ms. Diamond has served in various roles at Y&R since joining the firm in 1991, including Director of Client Services. Before joining Y&R, she held various positions at Ted Bates Advertising, at Grey Advertising and at Foote Cone and Belding, an advertising agency.

Director qualifications:

Leadership and operational experience global managing partner for multinational clients of advertising agency and former managing director

H. Russell Frisby, Jr. has served as a director of PAETEC Holding since February 2007 and as a director of PAETEC Corp. since January 2007. Mr. Frisby is a partner in the Energy and Telecommunications Group of Stinson Morrison Hecker LLP, a law firm. Mr. Frisby s legal practice focuses on regulatory and corporate matters affecting entities in the communications, energy and technology areas, and for over 20 years he has represented clients in a wide variety of proceedings before the FCC, state utility commissions and federal courts. Before joining Stinson Morrison Hecker, Mr. Frisby was a partner with the law firms Fleischman and Harding LLP and Kirkpatrick & Lockhart Nicholson Graham LLP. From February 1998 to March 2005, Mr. Frisby was the President, Chief Executive Officer and Acting Chief Legal Officer of the Competitive Telecommunications Association (CompTel). Before his service in that position, he served as Chairman of the Maryland Public Service Commission.

Director qualifications:

Leadership and industry experience former CEO and chief legal officer of industry association and currently a law firm partner focusing on communications, energy and technology areas

Tansukh V. Ganatra has served as a director of PAETEC Holding since February 2007. Mr. Ganatra co-founded US LEC in June 1996, served as a director of US LEC from June 1996 to February 2007 and served as interim Chief Executive Officer of US LEC from November 2006 to February 2007. He served as Chief Executive Officer and Vice Chairman of the board of directors of US LEC from July 1999 until his retirement in December 2001. Mr. Ganatra also served as President and Chief Operating Officer of US LEC from June 1996 until July 1999. From 1987 to 1997, Mr. Ganatra held various positions with ACC Corp., including service as its President and Chief Operating Officer. Before joining ACC, Mr. Ganatra held various positions during a 19-year career with Rochester Telephone Corporation, now known as Frontier Communications Corporation, a subsidiary of Citizens Communications Company, culminating with the position of Director of Network Engineering.

Director qualifications:

Leadership, industry and finance experience former CEO and other senior positions with telecommunications companies over four decades

Table of Contents

Michael C. Mac Donald has served as a director of PAETEC Holding since February 2007 and as Lead Director since March 2010. Mr. Mac Donald is currently retired. He served as a director of US LEC from April 2003 to February 2007. Before his retirement on December 31, 2009, Mr. Mac Donald held various sales and marketing positions with Xerox Corporation, a provider of document management technology and services, beginning in 1977. These positions included President of Xerox Marketing Operations and, most recently prior to his retirement, Senior Vice President, Operational Effectiveness. Mr. Mac Donald is a director of Medifast, Inc. and of the Jimmy V Foundation.

Director qualifications:

Leadership, finance and operational experience former senior executive sales and marketing positions with a public technology company focused on enterprise customer sales

William R. McDermott has served as a director of PAETEC Holding since February 2007 and as a director of PAETEC Corp. since March 2004. Mr. McDermott is the co- Chief Executive Officer of SAP AG, a provider of business software solutions headquartered in Walldorf, Germany. In this capacity, and also as a member of the Executive Board of SAP, he oversees SAP s strategic business activities relating to sales, all customer operations and ecosystem activities. Before joining SAP, Mr. McDermott served as the Executive Vice President, Worldwide Sales & Operations of Siebel Systems, a business software provider, as President of Gartner, Inc., a provider of research and analysis on the information technology industry, and on the boards of directors of two subsidiaries of Xerox Corporation. Mr. McDermott is also a director of Under Armour, Inc. and Ansys, Inc.

Director qualifications:

Leadership, finance and operational experience Co-CEO of a technology company

Alex Stadler has served as a director of PAETEC Holding since June 2008. Mr. Stadler previously served on the board of directors of McLeodUSA Incorporated from January 2006 until its acquisition by PAETEC Holding on February 8, 2008. From 1999 until 2002, he served as Chief Executive Officer of Riodata NV, a data services carrier specializing in private network and Internet access and connectivity for medium-sized companies. A wholly-owned subsidiary of Riodata NV filed for bankruptcy protection under the laws of Germany during the time that Mr. Stadler served as an officer for its controlling shareholder. Before joining Riodata NV, Mr. Stadler served as Chief Operating Officer of Otelo Communications, a competitive local exchange carrier, and as Chief Executive Officer of RWE Telliance AG, a German telecommunications company. Mr. Stadler joined GTE Corporation in 1977, and from 1985 to 1996 served in a variety of senior management positions at GTE s cellular and telephone subsidiaries and as GTE s head of mergers and acquisitions. Since 2002, Mr. Stadler has pursued private interests. Mr. Stadler started his career as an Economist at the Reserve Bank of Rhodesia.

Director qualifications:

Leadership and industry experience former CEO and other senior executive positions with technology and telecommunications companies

Finance experience former economist

Mark Zupan has served as a director of PAETEC Holding since February 2007 and as a director of PAETEC Corp. since May 2006. Mr. Zupan is dean of the William E. Simon Graduate School of Business Administration at the University of Rochester, a position which he has held on a full-time basis since January 1, 2004. Mr. Zupan previously served as dean and professor of economics at the University of Arizona s Eller College of Management from 1997 to 2003. Before his appointment at the University of Arizona, Mr. Zupan taught at the University of Southern California s Marshall School of Business, where he also served as associate dean of master degree programs. He was a teaching fellow in Harvard University s Department of Economics while pursuing his doctoral studies at the Massachusetts Institute of Technology, and has been a visiting faculty member at the Amos Tuck School of Business Administration at Dartmouth College. Mr. Zupan is also a director of Constellation Brands, Inc and served from 2003 to 2005 as a director of StockerYale, Inc.

86

Table of Contents

Director qualifications:

Finance experience academic specialty in finance and dean of a graduate school of business administration

Board of Directors

Director Qualifications. We believe that individuals who serve on our board of directors should demonstrate the requisite expertise, business acumen and experience to make a significant contribution to PAETEC; should display maturity of judgment and have the highest ethical character; should not present conflicts of interest that might impede proper performance; should have sufficient time to devote to board matters; should exhibit the ability to work effectively and collegially with other board members; and should be committed to building long-term stockholder value. We seek board members that represent a diversity of professional viewpoints, background and experience in areas that are relevant to our activities. We identify and describe below some of the key experience, qualifications, attributes and skills our directors bring to the board that are important in light of our business and structure.

Leadership experience. We seek directors who possess extraordinary leadership qualities and the ability to identify and develop those qualities in others. We believe that individuals with long-term experience in significant leadership positions are likely to provide the vision and insight that our industry and our company demand. Such individuals demonstrate an in-depth and practical understanding of strategy, technology, risk management and the methods to drive efficiency and growth. Through their current or former service as top leaders at other organizations, they are able to provide deep market and operational knowledge and have cultivated professional relationships that benefit our company.

Industry experience. We seek directors with experience as senior executives or directors, or in other leadership positions, in the communications industry. A sophisticated understanding of the competitive, technological and regulatory issues confronting our business is critical to our success.

Finance experience. We believe that all directors should possess an understanding of finance and related reporting processes. We also seek directors who can qualify as an audit committee financial expert, as that term is defined in the SEC s rules.

Operational experience. We seek directors who have operational expertise as well as experience in the areas of sales, marketing and business development, particularly in connection with large businesses.

Size and Composition of Board of Directors. The size of our board of directors is determined by resolution of the board of directors, subject to requirements of PAETEC s certificate of incorporation and bylaws described below. As of the date of this prospectus, the board of directors had ten members. Under our certificate of incorporation and bylaws, the number of directors constituting the entire board of directors may not be fewer than four or more than 15 directors.

Classification of Board of Directors. Our certificate of incorporation provides that the PAETEC board of directors is to be divided into three classes of directors. The three classes, which are required to be as nearly equal in number as possible, are designated Class I, Class II and Class III. As a result, approximately one-third of the board of directors is elected each year. Messrs. Frisby and Mac Donald and Ms. Diamond are Class I directors with a term expiring at our annual meeting of stockholders in 2013. Messrs. Ganatra, McDermott and Zupan are Class II directors with a term expiring at our annual meeting of stockholders in June 2011. Each of Messrs. Ganatra, McDermott and Zupan has been nominated for re-election to a new three-year term at such annual meeting. Messrs. Aab, Chesonis, Stadler and Wilson are Class III directors with a term expiring at our annual meeting of stockholders in 2012.

Table of Contents

Board Membership Agreement. In connection with the completion on February 8, 2008 of PAETEC s acquisition of McLeodUSA, PAETEC entered into a board membership agreement, dated as of February 8, 2008, which it amended as of March 10, 2008, with former stockholders of McLeodUSA consisting of investment funds managed by Wayzata Investment Partners LLC, which we refer to as the Wayzata funds, and investment funds and entities advised by Fidelity Management & Research Company and its affiliates, which we refer to as the Fidelity funds. The board membership agreement provided for, among other things, the right for the Wayzata funds to designate to PAETEC one representative for appointment or nomination to the board of directors and the right for the Fidelity funds to appoint one representative to attend each meeting of PAETEC s board of directors as a non-voting observer. In accordance with these provisions, in June 2008, the PAETEC board of directors appointed Alex Stadler to serve as the director representative of the Wayzata funds, and in October 2008, the Fidelity funds designated Richard J. Santagati to serve as an observer. Mr. Stadler subsequently was elected by the PAETEC stockholders at the 2009 annual meeting to serve as a Class III director for a term of three years. The rights of the Wayzata funds and the Fidelity funds under the board membership agreement with respect to board representation and non-voting board observer status terminated on February 8, 2010.

Director Independence. PAETEC s board of directors has determined that the following seven of its ten directors are independent directors within the meaning of the NASDAQ Marketplace Rules: Shelley Diamond; H. Russell Frisby, Jr.; Tansukh V. Ganatra; Michael C. MacDonald; William R. McDermott; Alex Stadler; and Mark Zupan. In making this determination, the board of directors concluded that none of those directors had any relationships which, in the board s opinion, would interfere with the director s exercise of independent judgment in carrying out the responsibilities of a director.

Compensation Committee Interlocks and Insider Participation. No member of the compensation committee of PAETEC S board of directors during 2010 is or has been an officer or employee of PAETEC or any subsidiary of PAETEC and no member of the compensation committee had any relationships requiring disclosure under the SEC s rules regarding transactions with related persons. In addition, during 2010, no member of the compensation committee or board of directors was an executive officer of another entity on whose board of directors a PAETEC executive officer serves.

Compensation of Directors

Directors who are also PAETEC officers or employees do not receive any compensation for serving on PAETEC s board of directors or any of its committees. Mr. Chesonis and Mr. Wilson are the only directors who serve as officers and employees of PAETEC.

The following policies regarding compensation of non-employee directors applied from January 1, 2010 through June 30, 2010:

- the audit committee chairman was entitled to annual cash fees of $80,000 and an annual grant of stock options for 12,500 shares of common stock and restricted stock units for 12,500 shares of common stock;

- the other audit committee members were entitled to annual cash fees of $60,000 and an annual grant of stock options for 9,500 shares of common stock and restricted stock units for 9,500 shares of common stock;

- the compensation committee chairman was entitled to annual cash fees of $70,000 and an annual grant of stock options for 10,500 shares of common stock and restricted stock units for 10,500 shares of common stock;

- the other compensation committee members were entitled to annual cash fees of $55,000 and an annual grant of stock options for 8,500 shares of common stock and restricted stock units for 8,500 shares of common stock;

- directors who do not serve on any board committees were entitled to annual cash fees of $50,000 and an annual grant of stock options for 7,500 shares of common stock and restricted stock units for 7,500 shares of common stock; and

- the Vice Chairman was entitled to annual cash fees of $70,000 and an annual grant of stock options for 10,500 shares of common stock and restricted stock units for 10,500 shares of common stock.

In 2010, the board of directors formed a nominating and governance committee and appointed a Lead Director. Thus, effective as of July 1, 2010, the following policies apply with respect to compensation of non-employee directors:

- the Lead Director, who also serves as the chairman of the nominating and governance committee and as a member of the audit committee, is entitled to annual cash fees of $100,000 and an annual grant of stock options for 15,000 shares of common stock and restricted stock units for 15,000 shares of common stock;

- the nominating and governance committee non-chairman member serving solely on that committee is entitled to annual cash fees of $55,000 and an annual grant of stock options for 8,500 shares of common stock and restricted stock units for 8,500 shares of common stock;

- the audit committee chairman is entitled to annual cash fees of $80,000 and an annual grant of stock options for 12,500 shares of common stock and restricted stock units for 12,500 shares of common stock;

- the audit committee non-chairman member serving solely on that committee is entitled to annual cash fees of $60,000 and an annual grant of stock options for 9,500 shares of common stock and restricted stock units for 9,500 shares of common stock;

- the compensation committee chairman is entitled to annual cash fees of $70,000 and an annual grant of stock options for 10,500 shares of common stock and restricted stock units for 10,500 shares of common stock;

- the compensation committee non-chairman member serving solely on that committee is entitled to annual cash fees of $55,000 and an annual grant of stock options for 8,500 shares of common stock and restricted stock units for 8,500 shares of common stock;

- the director serving as a member of both the compensation committee and the nominating and governance committee is entitled to annual cash fees of $60,000 and an annual grant of stock options for 9,500 shares of common stock and restricted stock units for 9,500 shares of common stock; and

- the Vice Chairman is entitled to annual cash fees of $70,000 and an annual grant of stock options for 10,500 shares of common stock and restricted stock units for 10,500 shares of common stock.

Non-employee directors also receive an equity award in connection with their appointment to the board of directors. All cash fees are payable in four equal quarterly installments in arrears. All equity grants vest with respect to one-third of the underlying shares of common stock on each of the first, second and third anniversaries of the grant date.

All directors are reimbursed for their reasonable out-of-pocket expenses incurred in connection with their board service. In addition, Mr. Ganatra is entitled to participate in the company s medical, dental and vision healthcare plans under which the company covers a portion of the premiums.

Table of Contents

The table below shows the compensation paid to our non-employee directors in 2010.

2010 Director Compensation Table

Name	Fees Earned or Paid in Cash ($)	Stock Awards ($)[1]	Option Awards ($)[1]	All Other Compensation ($)	Total ($)
Richard T. Aab[2]	70,000	41,055	28,044		139,099
Shelley Diamond[3]	56,250	37,455	25,575		119,280
H. Russell Frisby, Jr.[4]	52,500	33,235	22,703		108,438
Tansukh V. Ganatra[5]	60,000	37,145	25,374	10,782	133,301
Michael C. Mac Donald[6]	80,000	60,355	41,173		181,528
William R. McDermott[7]	70,000	41,055	28,044		139,099
Alex Stadler[8]	52,500	33,545	22,904		108,949
Mark Zupan[9]	80,000	48,875	33,386		162,261

(1) Amounts shown in the Stock Awards and Option Awards columns reflect the aggregate grant date fair value of stock or option awards granted in 2010 calculated in accordance with Financial Accounting Standards Board Accounting Standards Codification Topic 718, *Compensation-Stock Compensation*, or ASC 718. Assumptions used in the calculation of these amounts are set forth in Note 9 to PAETEC s audited consolidated financial statements appearing elsewhere in this prospectus.

(2) Mr. Aab served as Vice Chairman of the Board of Directors in 2010. As of December 31, 2010, Mr. Aab held unvested restricted stock units for 21,167 shares of common stock and options to purchase 34,500 shares of common stock, of which options to purchase 13,333 shares were vested.

(3) Shelley Diamond served as a member of the compensation committee and of the nominating and governance committee in 2010. As of December 31, 2010, Ms. Diamond held unvested restricted stock units for 12,834 shares of common stock and options to purchase 89,500 shares of common stock, of which options to purchase 20,416 shares were vested.

(4) Mr. Frisby served as a member of the compensation committee in 2010. As of December 31, 2010, Mr. Frisby held unvested restricted stock units for 15,167 shares of common stock and options to purchase 141,892 shares of common stock, of which options to purchase 96,293 shares were vested.

(5) Mr. Ganatra served as a member of the audit committee in 2010. As of December 31, 2010, Mr. Ganatra held unvested restricted stock units for 18,834 shares of common stock and options to purchase 30,500 shares of common stock, of which options to purchase 11,666 shares were vested. In connection with Mr. Ganatra s participation as a director in the PAETEC medical, dental and vision healthcare plans, PAETEC incurred a cost for premiums of $10,782.

(6) Mr. Mac Donald served as the Lead Director beginning in March 2010, and as a member of the nominating and governance committee and of the audit committee in 2010. As of December 31, 2010, Mr. Mac Donald held unvested restricted stock units for 23,000 shares of common stock and options to purchase 28,000 shares of common stock, of which options to purchase 5,000 shares were vested.

(7) Mr. McDermott served as the chairman of the compensation committee in 2010. As of December 31, 2010, Mr. McDermott held unvested restricted stock units for 21,167 shares of common stock and options to purchase 64,932 shares of common stock, of which options to purchase 43,765 were vested.

(8) Mr. Stadler served as a member of the nominating and governance committee in 2010. As of December 31, 2010, Mr. Stadler held unvested restricted stock units for 15,167 shares of common stock and options to purchase 176,800 shares of common stock, of which options to purchase 105,383 shares were vested.

(9) Mr. Zupan served as the chairman of the audit committee in 2010. As of December 31, 2010, Mr. Zupan held unvested restricted stock units for 25,834 shares of common stock and options to purchase 164,225 shares of common stock, of which options to purchase 138,391 shares were vested.

Table of Contents

The table below shows the grant date fair value of each stock option award and each restricted stock unit award granted to our non-employee directors in 2010, as computed in accordance with ASC 718.

2010 Director Equity Awards Table