BELLSOUTH CORP
Form 10-Q
November 05, 2001

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549

FORM 10-Q
(Mark One)

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

For the quarterly period ended September 30, 2001

OR

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

For the transition period from ___ to ___

Commission file number 1-8607

BELLSOUTH CORPORATION
(Exact name of registrant as specified in its charter)

Georgia (State of Incorporation)	58-1533433 (I.R.S. Employer Identification Number)
1155 Peachtree Street, N. E., Atlanta, Georgia (Address of principal executive offices)	30309-3610 (Zip Code)

Registrant's telephone number 404 249-2000

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

At October 31, 2001, 1,876,968,949 common shares were outstanding.

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PART I - FINANCIAL INFORMATION

BELLSOUTH CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)
(In Millions, Except Per Share Amounts)

	For the Three Months Ended September 30, 2000	2001	For the Nine Months Ended September 30, 2000	2001
Operating revenues:				
Communications group	$ 4,565	$ 4,770	$ 13,679	$14
Domestic wireless	963	-	2,766	
Latin America	757	710	2,124	2
Domestic advertising and publishing	539	493	1,329	1
All other	26	40	93	
Total operating revenues	6,850	6,013	19,991	17
Operating expenses:				
Operational and support expenses	3,612	3,138	10,647	9
Depreciation and amortization	1,301	1,178	3,759	3
Severance accrual	-	-	78	
Total operating expenses	4,913	4,316	14,484	13
Operating income	1,937	1,697	5,507	4
Interest expense	344	304	982	
Gain (loss) on sale of operations	(14)	24	(14)	
Net earnings of equity affiliates	10	167	163	
Other income (loss), net	35	(1,527)	164	(1

Income before income taxes	1,624	57	4,838	2
Provision for income taxes	588	50	1,737	1
Net income	$ 1,036	$ 7	$ 3,101	$ 1
Weighted-average common shares outstanding:				
Basic	1,871	1,875	1,878	1
Diluted	1,885	1,887	1,894	1
Dividends declared per common share	$ 0.19	$ 0.19	$ 0.57	$
Earnings per share:				
Basic	$ 0.55	$ 0.00	$ 1.65	$
Diluted	$ 0.55	$ 0.00	$ 1.64	$

The accompanying notes are an integral part of these consolidated financial statements.

BELLSOUTH CORPORATION
CONSOLIDATED BALANCE SHEETS
(In Millions, Except Per Share Amounts)

	December 31, 2000	September 30, 2001 (Unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1,061	$ 854
Accounts receivable, net of allowance for uncollectibles of $377 and $428	5,157	5,132
Material and supplies	379	377
Other current assets	809	950
Total current assets	7,406	7,313
Investments and advances	11,010	10,546
Property, plant and equipment	60,912	63,882
Less: accumulated depreciation	36,755	38,649
Property, plant and equipment, net	24,157	25,233
Deferred charges and other assets	4,180	4,876
Intangible assets, net	4,172	4,273
Total assets	$ 50,925	$ 52,241

LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Debt maturing within one year	$ 7,569	$ 6,961
Accounts payable	2,233	1,613
Other current liabilities	3,468	4,241
Total current liablities	13,270	12,815
Long-term debt	12,463	13,105
Noncurrent liabilities:		
Deferred income taxes	3,580	3,290
Other noncurrent liabilities	4,700	4,991
Total noncurrent liabilities	8,280	8,281
Shareholders' equity:		
Common stock, $1 par value (8,650 shares authorized; 1,872 and 1,877 shares outstanding)	2,020	2,020
Paid-in capital	6,740	6,766
Retained earnings	14,074	14,704
Accumulated other comprehensive loss	(488)	(277)
Shares held in trust and treasury	(5,222)	(5,034)
Guarantee of ESOP debt	(212)	(139)
Total shareholders' equity	16,912	18,040
Total liabilities and shareholders' equity	$ 50,925	$ 52,241

The accompanying notes are an integral part of these consolidated financial statements.

BELLSOUTH CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In Millions)

	For the Nine Months Ended September 30,	
	2000	2001
Cash Flows from Operating Activities:		
Net income	$ 3,101	$ 1,778
Adjustments to net income:		
Depreciation and amortization	3,759	3,538
Net losses on sale or impairment of equity securities	--	1,704

Postretirement benefit curtailment charge	--	72
Severance accrual	78	--
(Gain) loss on sale of operations	14	(24)
Provision for uncollectibles	278	370
Net losses (earnings) of equity affiliates	(163)	(357)
Dividends received from equity affiliates	55	279
Minority interests in income of subsidiaries	12	5
Deferred income taxes and investment tax credits	150	(343)
Net change in:		
Accounts receivable and other current assets	(529)	(505)
Accounts payable and other current liabilities	434	255
Deferred charges and other assets	(486)	(730)
Other liabilities and deferred credits	(60)	119
Other reconciling items, net	107	200
Net cash provided by operating activities	6,750	6,361
Cash Flows from Investing Activities:		
Capital expenditures	(4,940)	(4,724)
Investments in and advances to equity affiliates	(497)	(1,597)
Acquisitions, net of cash acquired	(1,836)	--
Purchases of wireless licenses	(72)	(10)
Proceeds from sale of investments	--	1,147
Proceeds from sale of operations	29	21
Proceeds from disposition of short-term investments	372	108
Purchases of short-term investments	(311)	(76)
Proceeds from repayment of loans and advances	45	25
Investments in debt securities	--	(279)
Other investing activities, net	60	1
Net cash used for investing activities	(7,150)	(5,384)
Cash Flows from Financing Activities:		
Net borrowings (repayments) of short-term debt	411	(1,405)
Proceeds from long-term debt	2,118	1,865
Repayments of long-term debt	(412)	(727)
Dividends paid	(1,072)	(1,068)
Purchase of treasury shares	(779)	--
Other financing activities, net	23	151
Net cash used for financing activities	289	(1,184)
Net decrease in cash and cash equivalents	(111)	(207)
Cash and cash equivalents at beginning of period	1,287	1,061
Cash and cash equivalents at end of period	$ 1,176	$ 854

The accompanying notes are an integral part of these consolidated financial statements.

BELLSOUTH CORPORATION
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
AND COMPREHENSIVE INCOME
(Unaudited)
(In Millions)

For the Nine Months Ended September 30, 2000

	Number of Shares		Amount				
	Common Stock	Shares Held in Trust and Treasury (a)	Common Stock	Paid-in Capital	Retained Earnings	Accum. Other Compre-hensive Income/ (Loss)	T T
Balance at December 31, 1999	2,020	(138)	$ 2,020	$ 6,771	$ 11,456	$ (358)	
Net income	-				3,101		
Other comprehensive income, net of tax:							
Foreign currency translation adjustment	-					50	
Net unrealized gains on securities	-					259	
Minimum pension liability adjustment	-					(9)	
Total comprehensive income (b)	-						
Dividends declared	-				(1,070)		
Share issuances for employee benefit plans	-	3			(66)		
Purchase of treasury stock	-	(19)					

Tax benefit related to stock options	-			4		
ESOP activities and related tax benefit	-					
Balance at September 30, 2000	2,020	(154)	$ 2,020	$ 6,775	$ 13,421	$ (58)

The accompanying notes are an integral part of these consolidated financial statements.

BELLSOUTH CORPORATION
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
AND COMPREHENSIVE INCOME
(Unaudited)
(In Millions)

For the Nine Months Ended September 30, 2001

	Number of Shares		Amount			
	Common Stock	Shares Held in Trust and Treasury (a)	Common Stock	Paid-in Capital	Retained Earnings	Accum. Other Compre-hensive Income/ (Loss)
Balance at December 31, 2000	2,020	(148)	$ 2,020	$ 6,740	$14,074	$(488)
Net income	-				1,778	
Other comprehensive income, net of tax:						
Foreign currency translation adjustment	-					(27)

Net unrealized losses on securities:							
Unrealized losses on securities	-					(241)	
Adjustments for other-than-temporary losses included in net income	-					525	
Net unrealized losses on derivatives	-					(46)	
Total comprehensive income (b)	-						
Dividends declared	-				(1,069)		
Share issuances for employee benefit plans	-	5		6	(81)		
Share issuances for Grantor Trust	-						
Tax benefit related to stock options	-			20			
ESOP activities and related tax benefit	-				2		
Balance at September 30, 2001	2,020	(143)	$ 2,020	$ 6,766	$14,704	$ (277)	

The accompanying notes are an integral part of these consolidated financial statements.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars In Millions)

Note A - Preparation of Interim Financial Statements

In this report, BellSouth Corporation and its subsidiaries are referred to as "we" or "BellSouth".

The accompanying unaudited consolidated financial statements have been prepared based upon Securities and Exchange Commission (SEC) rules that permit reduced disclosure for interim periods. In our opinion, these statements include all adjustments necessary for a fair presentation of the results of the interim periods shown. All adjustments are of a normal recurring nature unless otherwise disclosed. Revenues, expenses, assets and liabilities can vary during each quarter of the year. Therefore, the results and trends in these interim financial statements may not be the same as those for the full year. For a more complete discussion of our significant accounting policies and other information, you should read this report in conjunction with the consolidated financial statements included in our latest annual report on Form 10-K and previous quarterly reports on Form 10-Q.

Certain amounts within the prior year's information have been reclassified to conform to the current year's presentation.

Note B - New Accounting Pronouncements

BUSINESS COMBINATIONS AND GOODWILL AND OTHER INTANGIBLE ASSETS

In June 2001, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 141, "Business Combinations" and SFAS No. 142, "Goodwill and Other Intangible Assets". SFAS 141 requires the purchase method of accounting be used for all business combinations initiated after June 30, 2001. Use of the pooling-of-interests method is prohibited. SFAS 141 also provides new criteria to determine whether an acquired intangible asset should be recognized separately from goodwill.

Upon adoption of SFAS 142, amortization of existing goodwill would cease and the remaining book value would be tested for impairment at least annually at the reporting unit level using a new two-step impairment test. Amortization of goodwill recorded on equity investments would also cease, but this embedded goodwill will continue to be tested for impairment under current accounting rules for equity investments. In addition, we will have adjustments to the equity in net income of affiliates line item to reflect the impact of adopting these new statements on the operations of our equity investments.

We will adopt both statements on January 1, 2002 and are currently evaluating the impact of these statements. We have not yet quantified the impact of these statements on the operations of our equity investments, including Cingular and our Latin America group segment. Annual pre-tax amortization expense of our existing and embedded goodwill for 2001 will be $84. During 2002, we will perform the first of the required impairment tests of goodwill as of January 1, 2002, and we have not yet determined what the effect of these tests will be on our earnings and financial position. Any impairment resulting from our initial application of the statements will be recorded as a cumulative effect of accounting change as of January 1, 2002.

Derivative Instruments and Hedging Activities

SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" requires that entities recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. Gains and losses resulting from changes in the fair values of those derivatives are to be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. We adopted SFAS No. 133 on January 1, 2001. The impact of implementation was not material. The fair value of derivative instruments at September 30, 2001 was $(72).

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note C - Earnings Per Share

Basic earnings per share is computed on the weighted-average number of common shares outstanding during each period. Diluted earnings per share is based on the weighted-average number of common shares outstanding plus net incremental shares arising out of employee stock options and benefit plans. The following is a reconciliation of the weighted-average share amounts (in millions) used in calculating earnings per share:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2000	2001	2000	2001
Basic common shares outstanding	1,871	1,875	1,878	1,874
Incremental shares from stock options and benefit plans	14	12	16	12
Diluted common shares outstanding	1,885	1,887	1,894	1,886

The earnings amounts used for per-share calculations are the same for both the basic and diluted methods. Outstanding options for 52 million shares for the three months ended September 30, 2001 and 50 million for the nine months ended September 30, 2001 were not included in the computation of diluted earnings per share because the exercise price of these options was greater than the average market price of the common stock. Outstanding options for 33 million and 29 million shares were excluded for the same reason for the quarter and year-to-date 2000 periods, respectively.

Note D - Sale of Qwest Shares

In January 2001, we sold approximately 22.2 million shares of Qwest Communications common stock to Qwest for $1.0 billion in cash, or $45 per share.

In addition, we entered into an agreement to purchase $250 of services and products from Qwest over a five-year period, with payment being made in shares of Qwest stock we currently own. Accordingly, 5.3 million shares are considered restricted and are no longer classified as available-for-sale. Minimum payments under the agreement are required to be made annually. The stock prices used to compute the number of shares for such payments is fixed per the agreement. All such prices are above our original cost.

In July 2001, we sold an additional 4.5 million shares of Qwest common stock for $135 in cash, or $30 per share.

Note E - Restructuring of Wireless Video Entertainment Business

In December 2000, we announced that we would restructure our video entertainment service and concentrate our entertainment business on our fiber optic-based wireline video operations. This move was made to better align our resources with our strategic priorities in broadband services.

We recorded charges of approximately $498, or $323 net of tax, related to this restructuring in the fourth quarter of 2000. These charges consisted of approximately $289 for asset writeoffs and writedowns and $209 for contract termination penalties, migration of customers to alternative service providers and for severance and related benefit expenses. As of September 30, 2001, we have charged $156 against the $209 accrued, leaving the accrual at $53 as of that date. We expect to substantially complete the plan by the end of 2001. Operating revenues generated by this business were $15 in third quarter 2000 and $3 in third quarter 2001, while operating losses were $25 in third quarter 2000 and $9 in third quarter 2001. For the year-to-date periods, operating revenues were $43 in 2000 and $22 in 2001, while operating losses were $75 in 2000 and $25 in 2001.

Note F - Curtailment charge

In first quarter 2001, we recognized a curtailment loss of $72 in accordance with provisions of SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pension". The loss resulted from accelerated

Note F - Curtailment charge (continued)

recognition of prior service cost in excess of the decrease in our postretirement benefit obligation for the wireless employees that will be covered under Cingular's postretirement benefit plans.

Note G - Contribution of AB Cellular to Cingular

In December 2000, we exercised our option to redeem AT&T's 55.6% partnership interest in AB Cellular through the distribution of our Los Angeles Cellular operations to AT&T. This redemption resulted in our ownership of the remaining AB Cellular investment, including 100% of the Houston cellular operations, 87.35% of the Galveston cellular operations, and approximately $1,100 of cash. In January 2001, we received FCC approval and transferred these properties and the cash to Cingular, as contemplated by the October 2, 2000 Cingular contribution and formation agreement.

Note H - Segment Information

We have four reportable operating segments: (1) Communications group; (2) Domestic wireless; (3) Latin America; and (4) Domestic advertising and publishing. We have included the operations of all other businesses falling below the reporting threshold in the "All other" segment. The "Reconciling items" shown below include Corporate Headquarters and capital funding activities, the reversal of our proportionate share of Cingular's reported results, intercompany eliminations and other special items that may arise. Special items are transactions or events that are included in reported consolidated results but are excluded from segment results due to their nonrecurring or nonoperational nature.

During fourth quarter 2000, we contributed our domestic wireless operations to Cingular, and we account for our investment in Cingular under the equity method. For management purposes, however, we evaluate our domestic wireless segment based on our proportionate share of Cingular's results. Accordingly, the operating revenues and expenses reported for our domestic wireless segment for third quarter and year-to-date 2001 reflect 40% of Cingular's total revenues and expenses, whereas third quarter and year-to-date 2000 reflect the historical results of our wireless businesses that have been contributed to Cingular.

The following table provides information for each operating segment:

	For the Three Months Ended September 30, 2000	2001	% Change	For the Nine Mont Ended September 3 2000	200
Communications group					
External revenues	$ 4,539	$4,770	5.1	$ 13,601	$ 1
Intersegment revenues	99	37	(62.6)	280	
Total revenues	$ 4,638	$4,807	3.6	$ 13,881	$ 1
Operating income	$ 1,508	$1,354	(10.2)	$4,552	$
Segment net income	$ 837	$ 766	(8.5)	$2,540	$
Domestic wireless					
External revenues	$ 1,061	$1,465	38.1	$3,033	$
Intersegment revenues	10	-	N/M*	24	
Total revenues	$ 1,071	$1,465	36.8	$3,057	$
Operating income	$ 144	$ 291	102.1	$ 359	
Net earnings (losses) of equity affiliates	$ 41	$ -	N/M	$ 121	
Segment net income	$ 98	$ 128	30.6	$ 245	

* Not Meaningful

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note H - Segment Information (continued)

	For the Three Months Ended September 30, 2000	2001	% Change	For the Nine M Ended Septemb 2000
Latin America				
External revenues	$ 757	$ 710	(6.2)	$2,124
Intersegment revenues	15	6	(60.0)	47

Total revenues	$ 772	$ 716	(7.3)	$2,171
Operating income	$ 24	$ 86	258.3	$ 64
Net earnings (losses) of equity affiliates	$ (19)	$ (50)	N/M	$ (61)
Segment net income (loss)	$ (62)	$ (52)	N/M	$ (116)
Domestic advertising and publishing				
External revenues	$ 539	$ 493	(8.5)	$1,329
Intersegment revenues	6	3	(50.0)	17
Total revenues	$ 545	$ 496	(9.0)	$1,346
Operating income	$ 293	$ 257	(12.3)	$ 652
Segment net income	$ 181	$ 158	(12.7)	$ 399
All other				
External revenues	$ 21	$ 28	33.3	$ 69
Intersegment revenues	2	7	N/M	5
Total revenues	$ 23	$ 35	52.2	$ 74
Operating income	$ 8	$ 6	N/M	$ 13
Net earnings (losses) of equity affiliates	$ (12)	$ 14	N/M	$ 22
Segment net income (loss)	$ (10)	$ 18	N/M	$ 23
Reconciling items				
External revenues	$ (67)	$(1,453)	N/M	$ (165)
Intersegment revenues	(132)	(53)	N/M	(373)
Total revenues	$(199)	$(1,506)	N/M	$ (538)
Operating income (loss)	$ (40)	$ (297)	N/M	$ (133)
Net earnings (losses) of equity affiliates	$ -	$ 203	N/M	$ 81
Segment net income (loss)	$ (8)	$(1,011)	N/M	$ 10
Reconciliation to Consolidated Financial Information				
Operating Revenues				
Communications group	$ 4,638	$4,807	3.6	$ 13,881
Domestic wireless	1,071	1,465	36.8	3,057
Latin America	772	716	(7.3)	2,171
Domestic advertising and publishing	545	496	(9.0)	1,346
All other	23	35	52.2	74
Total segments	$ 7,049	$7,519	6.7	$ 20,529
Reconciling items	$(199)	$(1,506)	N/M	$ (538)
Total consolidated	$ 6,850	$6,013	(12.2)	$ 19,991

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note H - Segment Information (continued)

	For the Three Months Ended September 30,		%	For the Nine Mon Ended September	
	2000	2001	Change	2000	20
Reconciliation to Consolidated Financial Information, continued					
Net Income					

Communications group	$ 837	$ 766	(8.5)	$2,540	$
Domestic wireless	98	128	30.6	245	
Latin America	(62)	(52)	N/M	(116)	
Domestic advertising and publishing	181	158	(12.7)	399	
All other	(10)	18	N/M	23	
Total segments	$ 1,044	$1,018	(2.5)	$3,091	$
Reconciling items	$ (8)	$(1,011)	N/M	$ 10	$(
Total consolidated	$ 1,036	$ 7	(99.3)	$3,101	$

Note I - Investment Activity

Advance to Affiliate
(Euros in millions)
In August 2001, we loaned Euro 1,510, or $1,382, directly to E-Plus, an equity investment, with an expected March 1, 2004 due date, at LIBOR plus 310 basis points. E-Plus used the proceeds to pay down existing third party debt previously guaranteed by BellSouth. Simultaneously with this transaction, in order to mitigate foreign currency risk, we also entered into a forward contract to sell Euro with a March 1, 2004 settlement date. The forward, which qualifies as a cash flow hedge, enables us to receive $1,382 equivalent to Euro 1,510, based on a forward rate of 0.9158.

Note J - Marketable Securities

We have investments in marketable securities, primarily common stocks, which are accounted for under the cost method. These investments are comprised primarily of our equity interest in Qwest and are classified as available-for-sale under SFAS No. 115. Under SFAS No. 115, available-for-sale securities are required to be carried at their fair value, with unrealized gains and losses, net of income taxes, recorded in accumulated other comprehensive income (loss) in our statement of changes in shareholders' equity and comprehensive income. The fair values of our investments in marketable securities are determined based on market quotations. Equity securities that are restricted for more than one year or not publicly traded are recorded at cost.

Over the course of the year, there has been a broad decline in the public equity markets, particularly in technology and communications stocks, including investments held in our portfolio. Similarly, we experienced significant declines in the value of certain privately held investments and restricted securities. As a result, we recorded a $1,566 noncash pretax charge to reduce the carrying value of certain strategic investments in publicly traded and private equity securities, principally our investment in Qwest. We concluded that the continuing depressed market of these investments, as well as the difficulties experienced by similar companies, indicated that the decline was other than temporary. This charge is included in other income in the accompanying consolidated statements of income.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note J - Marketable Securities (continued)

The tables below show certain summarized information related to our investments that are adjusted to their fair value at September 30:

2000	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Recorded Basis
Investment in Qwest	$3,500	$ 65	$ --	$ 3,565
Other investments	482	146	--	628
Total	$3,982	$ 211	$ --	$ 4,193

2001	Original Cost	Gross Impairment Losses	Fair Value/ New Cost Basis
Investment in Qwest	$1,988	$(1,286)	$ 702
Other investments	500	(280)	220
Total	$2,488	$(1,566)	$ 922

Note K - Summary Financial Information for Equity Investees

The following table displays the summary combined financial information of our equity method businesses. These amounts are shown on a 100-percent basis.

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2000	2001	2000	2001
Revenues	$1,562	$4,713	$4,628	$13,819
Operating income ...	$80	$ 927	$ 364	$ 2,210
Net income	$(25)	$ 482	$ 47	$ 833

Note L- Debt Issuance

In April 2001, we privately sold $1,000 of 20-year annual put reset securities. The notes bear interest at 4.287% until April 2002, at which time the interest rate will be reset if certain investment banks holding call options exercise their options and remarket the notes. If the banks do not exercise their call options on that date, we will be required to redeem the notes at par. The proceeds were used to pay down short-term borrowings.

NOTE M - Sale of Operations

In July 2000, we sold our ownership interests in mobile data operations in Belgium, the Netherlands and the United Kingdom for total proceeds of $28. These sales generated a pre-tax net loss of $14 and a $30 after-tax gain resulting from tax benefits associated with the sale of the operations in the United Kingdom.

In August 2001, we sold our 24.5% ownership interest in SkyCell Communications, a wireless communications provider in India, for total proceeds of $21. The pretax gain on the sale was $24, or $19 after tax.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note N - Contingencies

Litigation Matters

Reciprocal compensation

Following the enactment of the Telecommunications Act of 1996, our telephone company subsidiary, BellSouth Telecommunications, Inc. (BST), and various competitive local exchange carriers entered into interconnection agreements providing for, among other things, the payment of reciprocal compensation for local calls initiated by the customers of one carrier that are completed on the network of the other carrier. Numerous competitive local carriers have claimed entitlement from BST for compensation associated with dial-up calls originating on BST's network and connecting with Internet service providers served by the competitive local carriers' networks. BST has maintained that dial-up calls to Internet service providers are not local calls for which terminating compensation is due under the interconnection agreements; however, the courts and state regulatory commissions in BST's operating territory that have considered the matter have, in most cases, ruled that BST is responsible for paying reciprocal compensation on these calls.

Also during the second quarter of 2001, the FCC released an Order on Remand and Report and Order addressing the issue of compensation for ISP traffic. In its Order, the FCC acknowledged that dial-up calls to Internet service providers are not local calls, but instead are "information access" traffic exempt from the reciprocal compensation provisions of the 1996 Act. The FCC has implemented a three-year interim period during which local carriers will pay inter-carrier compensation for such calls in decreasing increments. After the three-year interim period, the new rules on inter-carrier compensation to be adopted in connection with a Notice of Proposed Rulemaking released on April 27, 2001 are expected to be in effect. If no rules have been adopted by that time, the inter-carrier compensation in effect at the end of the third year would remain in effect.

During the second quarter of 2001, we adjusted our accrual for these claims. This adjustment increased our expenses by approximately $140 and reduced net income by $88. The adjustment reflects our current estimate of the liability for these claims. We have commenced discussions with several competitive local exchange carriers concerning settlement of these claims, and agreements have been reached in many circumstances.

Other reciprocal compensation issues
In a related matter, a competitive local carrier has claimed terminating compensation of approximately $165 for service arrangements that we did not

believe involved "traffic" under our interconnection agreements. We filed a complaint with the state regulatory commission asking that agency to declare that we did not owe reciprocal compensation for these arrangements. In March 2000, the state commission ruled in our favor finding that compensation was not owed to the competitive local carrier. The parties have agreed to a settlement of this matter. In October, a stipulation of dismissal was filed with the court to effect the settlement.

Compliance Matters

Foreign Corrupt Practices Act

In July 2000, the SEC began a formal investigation of whether we and others may have violated the Foreign Corrupt Practices Act (FCPA). The SEC has subpoenaed documents relating to the activities of our foreign subsidiaries, and we have produced responsive documents. Prior to the commencement of the SEC's formal investigation, we had engaged outside counsel to investigate an FCPA matter relating to the activities of one of our foreign subsidiaries in Latin America, and outside counsel concluded that those activities did not violate the Act. Thereafter and independent of these developments, our internal auditors, in the ordinary course of conducting compliance reviews, identified issues concerning accounting entries made by another of our Latin American subsidiaries. We have informed the SEC as to this matter, and the SEC has expanded its investigation to encompass it. Our internal investigation of the FCPA compliance of our foreign subsidiaries is continuing. We

Note N - Contingencies (continued)

are cooperating with the SEC in its investigation, but we cannot predict the duration or the outcome of the SEC's investigation or whether the scope of the investigation will be expanded beyond the matters currently identified.

Regulatory matters

Beginning in 1996, we operated under a price regulation plan approved by the South Carolina Public Service Commission under existing state laws. In April 1999, however, the South Carolina Supreme Court invalidated this price regulation plan. In July 1999, we elected to be regulated under a new state statute, adopted subsequent to the Commission's approval of the earlier plan. The new statute allows telephone companies in South Carolina to operate under price regulation without obtaining approval from the Commission. The election became effective during August 1999. The South Carolina Consumer Advocate petitioned the Commission seeking review of the level of our earnings during the 1996-1998 period when we operated under the subsequently invalidated price regulation plan. The Commission voted to dismiss the petition in November 1999 and issued orders confirming the vote in February and June of 2000. In July 2000, the Consumer Advocate appealed the Commission's dismissal of the petition.

Also in 2000, the Florida Public Service Commission issued a proposed agency action stating that our change in 1999 from a late charge based on a percentage of the amounts overdue to a flat rate fee plus an interest charge violated the

Florida price regulation statute and voted that approximately $65 should be refunded. We protested the decision. On August 30, 2001, the Commission issued an order adopting its proposed action. We have appealed to the Florida Supreme Court and continue to collect the charges subject to refund.

Other Claims

We are subject to claims arising in the ordinary course of business involving allegations of personal injury, breach of contract, anti-competitive conduct, employment law issues, regulatory matters and other actions. BST is also subject to claims attributable to pre-divestiture events involving environmental liabilities, rates, taxes, contracts and torts. Certain contingent liabilities for pre-divestiture events are shared with AT&T Corp. While complete assurance cannot be given as to the outcome of these claims, we believe that any financial impact would not be material to our results of operations, financial position or cash flows.

Note O - Tracking Stock

In December 2000, our shareholders approved amendments to our charter that will permit us to issue our common stock in series, and our Board of Directors intends to initially designate two series: Latin America group stock, intended to reflect the separate performance of our Latin American businesses, and BLS group stock, intended to reflect the separate performance of all of our other businesses.

We plan a public offering of shares of Latin America group stock to finance our expansion in Latin America. At the time of a public offering, a number of shares of Latin America group stock will be reserved for the BLS group or for issuance to the holders of BLS group stock. We expect that we would distribute, as a dividend to the holders of BLS group stock, the reserved shares of Latin America group stock within six to 12 months following the public offering.

Our plans to create, issue and distribute Latin America group stock are subject to a number of conditions, including market conditions and other factors. The implementation and timing of these transactions are uncertain.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note P - Subsidiary Financial Information

We have fully and unconditionally guaranteed all of the outstanding debt securities of BST that are subject to the reporting requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934. BST is a 100% owned subsidiary of BellSouth. In accordance with SEC rules, BST is no longer subject to the reporting requirements of the Securities Exchange Act of 1934, and we are providing the following condensed consolidating financial information.

BST is listed separately because it has debt securities, registered with the SEC, that we have guaranteed. All other operating subsidiaries that do not have registered securities guaranteed by us are presented in the Other column. The Parent column is comprised of headquarter entities which provide, among other services, executive management, administrative support and financial management to operating subsidiaries. The Adjustments column includes the necessary amounts to eliminate the intercompany balances and transactions between BST, Other and Parent to reconcile to our consolidated financial information.

CONDENSED CONSOLIDATING STATEMENTS OF INCOME

	For the Three Months Ended Septe		
	BST	Other	Parent
Total operating revenues	$ 4,528	$ 2,646	$ 566
Total operating expenses	3,166	2,281	360
Operating income	1,362	365	206
Interest expense	179	81	266
Net earnings (losses) of equity affiliates	4	(5)	1,360
Other income (expense), net	1	-	220
Income before income taxes	1,188	279	1,520
Provision for (benefit from) income taxes	441	78	70
Net income	$ 747	$ 201	$ 1,450

	For the Three Months Ended Septe		
	BST	Other	Parent
Total operating revenues	$ 4,662	$ 1,536	$ 755
Total operating expenses	3,531	1,248	482
Operating income	1,131	288	273
Interest expense	140	40	213
Net earnings (losses) of equity affiliates	3	177	1,112
Other income (expense), net	4	(139)	(1,272)
Income before income taxes	998	286	(100)
Provision for income taxes	362	149	(529)
Net income	$ 636	$ 137	$ 429

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note P - Subsidiary Financial Information (continued)

	For the Nine Months Ended Septe		
	BST	Other	Parent
Total operating revenues	$ 13,547	$ 7,283	$ 1,321

Total operating expenses	9,498	6,485	686
Operating income	4,049	798	635
Interest expense	516	201	651
Net earnings (losses) of equity affiliates	11	149	3,925
Other income (expense), net	4	(27)	589
Income before income taxes	3,548	719	4,498
Provision for income taxes	1,307	223	204
Net income	$ 2,241	$ 496	$ 4,294

	For the Nine Months Ended Septe		
	BST	Other	Parent
Total operating revenues	$ 13,895	$ 4,717	$ 1,947
Total operating expenses	10,277	4,033	1,414
Operating income	3,618	684	533
Interest expense	471	210	580
Net earnings (losses) of equity affiliates	11	353	3,386
Other income (expense), net	14	(48)	(1,029)
Income before income taxes	3,172	779	2,310
Provision for (benefit from) income taxes	1,146	441	(569)
Net income	$ 2,026	$ 338	$ 2,879

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note P - Subsidiary Financial Information (continued)

CONDENSED CONSOLIDATING BALANCE SHEETS

	BST	Other	December 31, 2000 Parent	Adj
ASSETS				
Current assets:				
Cash and cash equivalents	$ 62	$ 999	$ -	
Accounts receivable, net	3,195	2,162	5,522	
Other current assets	271	837	184	
Total current assets	3,528	3,998	5,706	
Investments and advances	322	7,505	10,592	
Property, plant and equipment, net	21,277	2,518	362	
Deferred charges and other assets	3,868	219	186	
Intangible assets, net	692	3,291	189	
Total assets	$ 29,687	$ 17,531	$ 17,035	
LIABILITIES AND SHAREHOLDERS' EQUITY				
Current liabilities:				
Debt maturing within one year	$ 1,830	$ 1,724	$ 8,791	
Other current liabilities	3,514	4,054	1,105	
Total current liablities	5,344	5,778	9,896	
Long-term debt	7,641	1,594	8,139	
Noncurrent liabilities:				
Deferred income taxes	2,306	1,271	3	
Other noncurrent liabilities	3,209	1,316	321	
Total noncurrent liabilities	5,515	2,587	324	
Shareholders' equity	11,187	7,572	(1,324)	
Total liabilities and shareholders' equity	$ 29,687	$ 17,531	$ 17,035	

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note P - Subsidiary Financial Information (continued)

	September 30, 2001				
	BST	Other	Parent	Adjustments	Total
ASSETS					
Current assets:					
Cash and cash equivalents	$ -	$ 500	$ 354	$ -	$ 854
Accounts receivable, net	3,339	2,103	3,433	(3,743)	5,132
Other current assets	377	649	334	(33)	1,327
Total current assets	3,716	3,252	4,121	(3,776)	7,313
Investments and advances	303	5,838	7,675	(3,270)	10,546
Property, plant and equipment, net	22,155	2,583	495	-	25,233
Deferred charges and other assets	4,626	194	128	(72)	4,876
Intangible assets, net	946	3,100	213	14	4,273
Total assets	$ 31,746	$ 14,967	$ 12,632	$ (7,104)	$ 52,241
LIABILITIES AND SHAREHOLDERS' EQUITY					
Current liabilities:					
Debt maturing within one year	$ 2,654	$ 459	$ 6,655	$ (2,807)	$ 6,961
Other current liabilities	3,664	1,894	1,182	(886)	5,854
Total current liablities	6,318	2,353	7,837	(3,693)	12,815
Long-term debt	7,589	2,327	5,964	(2,775)	13,105
Noncurrent liabilities:					
Deferred income taxes	2,624	1,166	(553)	53	3,290
Other noncurrent liabilities	3,376	1,388	369	(142)	4,991
Total noncurrent liabilities	6,000	2,554	(184)	(89)	8,281
Shareholders' equity:	11,839	7,733	(985)	(547)	18,040
Total liabilities and shareholders' equity	$ 31,746	$ 14,967	$ 12,632	$ (7,104)	$ 52,241

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note P - Subsidiary Financial Information (continued)

CONDENSED CONSOLIDATING CASH FLOW STATEMENTS

	For the Nine Months Ended September 30, 2000			
	BST	Other	Parent	Adjustments
Cash flows from operating activities	$4,861	$ 1,760	$ 5	$ 124

Cash flows from investing activities	(3,654)	(2,170)	(3,445)	2,119
Cash flows from financing activities	(1,148)	593	3,087	(2,243
Net increase (decrease) in cash	$ 59	$ 183	$ (353)	$ -

	For the Nine Months Ended September 30, 2001			
	BST	Other	Parent	Adjustments
Cash flows from operating activities	$4,605	$ 1,218	$ (629)	$ 1,167
Cash flows from investing activities	(3,948)	(744)	(1,102)	409
Cash flows from financing activities	(719)	(582)	1,693	(1,576
Net increase (decrease) in cash	$ (62)	$ (108)	$ (37)	$ -

Note Q - Other Matters

CWA AGREEMENT

In August 2001, we reached an agreement with the Communications Workers of America (CWA), which was ratified in September 2001, on new three-year contracts covering approximately 56,000 employees. The contracts include basic wage increases totaling 13% over the three years covered by the contracts. In addition, the agreement provides for a standard award of two percent of base salary and overtime compensation which is subject to adjustment based on company performance measures for plan years 2002 and 2003. Other terms of the agreement include pension band increases and pension plan cash balance improvements for active employees.

Note R - Subsequent Events

In October 2001, we filed applications with the Federal Communications Commission to offer long distance service to customers in Louisiana and Georgia. These filings followed the unanimous approval by the Public Service Commissions (PSC) in Louisiana (September 19) and Georgia (October 2). In October 2001, the Mississippi PSC unanimously endorsed BellSouth's state-level filing to provide long distance service.

In October 2001, we announced that we would record an after-tax charge of $170 to $200, or $0.09 to $0.10 per share, during the fourth quarter reflecting restructuring actions and related asset impairments. These actions are being taken to reduce operating costs in response to a slowing economy and increased competition. Targeted reductions will be largely focused on staff support functions, resulting in the elimination of approximately 3,000 positions.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)
(Dollars In Millions)

Note R - Subsequent Events (continued)

In October 2001, we issued long term notes of $1,000, $1,000, and $750 with interest rates of 5%, 6%, and 6.875%, respectively and maturing October 2006, 2011, and 2031, respectively. The net proceeds of $2,725 were used to pay down commercial paper.

In October 2001, we loaned Euro 525 million, or $468, directly to E-Plus, an equity investment, with an expected March 1, 2004 due date, at LIBOR plus 310 basis points. E-Plus used the proceeds to pay down existing third party debt previously guaranteed by BellSouth. Simultaneously with this transaction, in order to mitigate foreign currency risk, we also entered into a forward contract to sell Euro with a March 1, 2004 settlement date. The forward, which qualifies as a cash flow hedge under the scope of FAS 133, enables us to receive $468 equivalent to Euro 525 million, based on a forward rate of 0.8914.

BELLSOUTH CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS
(Dollars in Millions, Except Per Share Amounts)

For a more complete understanding of our industry, the drivers of our business and our current period results, you should read the following Management's Discussion and Analysis of Financial Condition and Results of Operations in conjunction with our latest annual report on Form 10-K, our previous quarterly reports on Form 10-Q, and our other filings with the SEC.

Consolidated Results of Operations

Key financial and operating data for third quarter 2000 and 2001 and the respective year-to-date periods are as follows. All references to earnings per share are on a diluted basis:

	For the Three Months Ended September 30, 2000	2001	% Change
Results of operations:			
Operating revenues	$6,850	$ 6,013	(12.2)
Operating expenses	4,913	4,316	(12.2)
Operating income	1,937	1,697	(12.4)
Interest expense	344	304	(11.6)
Net earnings (losses) of equity affiliates	10	167	N/M*
Gain (loss) on sale of operations	(14)	24	N/M
Other income, net	35	(1,527)	N/M
Provision for income taxes	588	50	(91.5)
Net income	$1,036	$ 7	(99.3)
Earnings per share	$ 0.55	$ 0.00	(100.0)

Cash flow data:			
Cash provided by operating activities	$ 1,952	$ 2,434	24.7
Cash used for investing activities	$(3,355)	$(2,695)	(19.7)
Cash provided by (used for) financing activities	$ 1,059	$ 457	N/M
Other:			
Effective tax rate	36.2%	87.7%	N/M
Average debt balances:			
Short-term debt	$7,019	$6,434	(8.3)
Long-term debt	$10,899	$13,123	20.4
Total average debt balance	$17,918	$19,557	9.1
EBITDA(1)	$3,238	$2,875	(11.2)
EBITDA margin(2)	47.3%	47.8%	+50 bps

	For the Nine Months Ended September 30, 2000	2001	% Change
Results of operations:			
Operating revenues	$ 19,991	$ 17,917	(10.4)
Operating expenses	14,484	13,069	(9.8)
Operating income	5,507	4,848	(12.0)
Interest expense	982	998	1.6
Net earnings (losses) of equity affiliates	163	357	N/M
Gain (loss) on sale of operations	(14)	24	N/M
Other income, net	164	(1,363)	N/M
Provision for income taxes	1,737	1,090	(37.2)
Net income	$3,101	$ 1,778	(42.7)
Earnings per share	$ 1.64	$0.94	(42.7)
Cash flow data:			
Cash provided by operating activities	$ 6,750	$ 6,361	(5.8)
Cash used for investing activities	$(7,150)	$(5,384)	(24.7)
Cash provided by (used for) financing activities	$ 289	$(1,184)	N/M
Other:			
Effective tax rate	35.9%	38.0%	+210 bps
Average debt balances:			
Short-term debt	$6,481	$ 6,332	(2.3)
Long-term debt	$10,608	$13,172	24.2
Total average debt balance	$17,089	$19,504	14.1
EBITDA(1)	$ 9,344	$8,386	(10.3)
EBITDA margin(2)	46.7%	46.8%	+10 bps

(1) EBITDA represents income before net interest expense, income taxes, depreciation and amortization, severance accrual, net earnings

(losses) of equity affiliates, gain (loss) on sale of operations and other income, net. We present EBITDA because it is a widely accepted financial indicator used by certain investors and analysts to analyze and compare companies on the basis of operating performance and because we believe that EBITDA is an additional meaningful measure of performance and liquidity. EBITDA does not represent cash flows for the period, nor is it an alternative to operating income (loss) as an indicator of operating performance. You should not consider it in isolation or as a substitute for measures of performance prepared in accordance with generally accepted accounting principles. The items excluded from the calculation of EBITDA are significant components in understanding and assessing our financial performance. Our computation of EBITDA may not be comparable to the computation of similarly titled measures of other companies. EBITDA does not represent funds available for discretionary uses.

(2) EBITDA margin is EBITDA divided by operating revenues.

* - Not meaningful.

Overview of consolidated results of operations

On a comparative basis, our results reflect the effects of the contribution of our former domestic wireless operations to Cingular Wireless in fourth quarter 2000, and our acquisition of operations in Colombia in July 2000.

The results for year-to-date 2000 include:

- Income related to the restructuring of our ownership interest in the German wireless operator, E-Plus, which increased net income by $68, or $0.04 per share.

- Expense recorded as a result of our previously announced plan to reduce our domestic general and administrative staff, which reduced net income by $48, or $0.03 per share.

The results for third quarter 2001 include:

- Losses related to the write down of our investments in equity securities, which reduced net income by $1,017, or $0.54 per share.

- Gain related to the sale of our 24.5% ownership interest in SkyCell Communications, which increased net income by $19, or $0.01 per share.

- A loss recorded as a result of selling 4.5 million shares of Qwest common stock, which reduced net income by $52, or $0.03 per share.

- Losses incurred as we exit our wireless video entertainment business, which reduced net income by $6 for the quarter and $16, or $0.01 per share, for the year-to-date period.

In addition to the third quarter items, the year-to-date 2001 period includes:

- Our adjustment to an accrual for reciprocal compensation, which reduced net income by $88, or $0.05 per share.

- A loss recorded as a result of selling an additional 22.2 million shares of Qwest common stock. We received total proceeds of $1,000 and recognized a loss of $50, or $32 after tax, or $0.02 per share.

- Expense recorded for changes in post retirement medical benefit obligations, which reduced net income by $47, or $0.02 per share.

Events Affecting Comparability

Formation of Cingular Wireless

In October 2000, we contributed our domestic wireless voice and data operations to a joint venture with SBC Communications and formed Cingular Wireless. We own an approximate 40% stake in Cingular, and share joint control with SBC. Accordingly, we account for our share of Cingular's results using the equity method. Prior to October 2000, we consolidated the revenues and expenses of these operations. As a result of this change, our third quarter and year-to-date 2000 results include the revenues and expenses attributable to our former domestic wireless operations and our third quarter and year-to-date 2001 results include equity in earnings attributable to Cingular.

Operating Revenues

Our reported operating revenues decreased $837 in third quarter 2001 and $2,074 for the year-to-date period compared to the same periods in 2000. These changes reflect:

- A decrease of $963 for the third quarter and $2,766 for the year-to-date period from our domestic wireless operations due to the contribution of our domestic wireless operations to Cingular, as explained above.

- Increases in our communications group of $205 for the third quarter and $520 for the year-to-date period driven by strong growth in digital and data revenues, wholesale revenues, and by the company's marketing of calling features. These increases were offset by declines in basic service revenues, reflecting competition and a slowing economy. Also impacting revenues was the decline in our public payphone business.

- Revenues from our Latin America group decreased $47 for the third quarter and increased $103 for the year-to-date period. The decrease for the quarter was driven by the impact of deteriorating foreign currencies in Latin America and an unfavorable change in the interconnection agreements at our Venezuelan operations. The year-to-date increase was driven by the acquisition of Colombia in June 2000. We added approximately 1.4 million customers quarter over quarter. The impact of customer additions on revenue growth was offset by declining monthly revenue per customer resulting from increased penetration of cellular service into the mass-consumer market and exchange rate declines in some countries.

- A decrease in revenues from our domestic advertising and publishing group of $46 for the third quarter driven by the timing of book publications. Revenues for the year-to-date period grew $34, or 2.6%, which were negatively impacted by slowing economic conditions, which have negatively impacted revenue growth.

Operating Expenses

Total operating expenses decreased $597 during third quarter 2001 and $1,415 during the year-to-date period. Operating expenses for year-to-date 2000 include a $78 severance accrual related to domestic general and administrative staff reductions. Operating expenses for year-to-date 2001 were impacted by approximately $140 of expense related to our adjustment of the accrual for reciprocal compensation. Operating expenses for year-to-date 2001 were also impacted by a curtailment loss related to postretirement medical benefits which increased expenses by $72. The decrease of $597 for the third quarter and the remaining decrease of $1,549 for the year-to-date period reflect:

- A decrease of $474 for the third quarter and $1,328 for the year-to-date period in operational and support expenses. Included in this change were decreases of $678 for the third quarter and $1,959 for the year-to-date period attributable to the domestic wireless operations which were contributed to Cingular. Offsetting these decreases were higher expenses in the communications group driven by our accelerated DSL growth initiative and customer service initiatives.

- A decrease of $123 for the third quarter and $221 for the year-to-date period in depreciation and amortization due primarily to $151 for the third quarter and $472 for the year-to-date period of expense recorded by our former domestic wireless operations in 2000. These decreases were offset by increases at the communications group reflecting increased deployment of capitalized software and investment in broadband since the third quarter of 2000.

Interest Expense

Interest expense decreased 11.6% in third quarter 2001 and increased 1.6% in year-to-date 2001 as compared to the same 2000 periods. Lower average interest rates on commercial paper were the primary reason for the third quarter decrease and reduced the impact of the year-to-date increase. The higher interest expense in the year-to-date period is attributed to higher average debt balances driven by increased debt related to increased investment acquisition activity.

Net Earnings (Losses) of Equity Affiliates

Earnings from our unconsolidated businesses increased $157 in third quarter 2001 and $194 for the year-to-date period. These increases were driven primarily by earnings in our equity investment in Cingular, which totaled $209 for the quarter and $563 for the year-to-date. Prior year quarter and year-to-date amounts include AB Cellular earnings of $39 and $114, respectively, which were subsequently contributed to Cingular. These net domestic wireless increases were offset by higher losses of $31 in the third quarter and $126 year-to-date from our equity investments in Latin America, driven by foreign exchange losses in Brazil. In addition, the year-to-date 2000 period results included $68 of income related to the restructuring of our ownership interest in our German wireless operations. These results are addressed in the discussions for the domestic wireless, Latin America group and all other segments.

Gain (loss) on Sale of Operations

In July 2000, we sold our ownership interest in mobile data operations in Belgium, the Netherlands and the United Kingdom. These sales generated a pre-tax net loss of $14.

In August 2001, we sold our 24.5% ownership interest in SkyCell Communications, a wireless communications provider in India. The pretax gain on the sale was $24.

Other Income

Other income, net includes interest income, gains/losses on disposition of assets, foreign currency gains/losses and miscellaneous nonoperating income. The decreases of $1,562 in third quarter 2001 and $1,527 for the year-to-date period were primarily driven by the pre-tax charge of $1,566 related to the write-down of certain investments to appropriately reflect their fair value.

Provision for Income Taxes

The provision for income taxes decreased $538 in third quarter 2001 and $647 for the year-to-date period. Our effective tax rate increased from 36.2% in third quarter 2000 to 87.7% in third quarter 2001. The increase in the effective tax rate was primarily driven by significantly lower pre-tax earnings as a result of the investment write down.

For the year-to-date period, the effective tax rate increased from 35.9% in 2000 to 38.0% in 2001. The increase in the effective tax rate is due primarily to the impact of the investment write down. These losses were recorded at corporate entities with full valuation allowances on state tax benefits. In addition, the effective tax rate was impacted by higher losses from our Brazilian equity investments, a one-time gain related to the restructuring of E-Plus in first quarter 2000 and increases in valuation allowances from foreign operations.

Results by Segment

We have four reportable operating segments: (1) Communications group; (2) Domestic wireless; (3) Latin America; and (4) Domestic advertising and publishing. We have included the operations of all other businesses falling below the reporting threshold in the "All other" segment. We evaluate the performance of each business unit based on net income, exclusive of charges for use of intellectual property and adjustments for special items that may arise. Special items are transactions or events that are included in reported consolidated results but are excluded from segment results due to their nonrecurring or nonoperational nature.

The following discussion highlights our performance in the context of these segments. For a more complete understanding of our industry, the drivers of our business, and our current period results, you should read this discussion in conjunction with our consolidated financial statements, including the related notes.

Communications Group

The communications group includes our core domestic businesses including: All domestic wireline voice, data, broadband, e-commerce, long distance, Internet services and advanced voice features. Services are marketed across three major customer segments: residential, business and wholesale.

	For the Three Months Ended September 30, 2000	2001	% Change
Results of Operations			
Operating revenues:			
Local service	$2,888	$3,003	4.0

Network access	1,154	1,252	8.5
Long distance	178	192	7.9
Other communications	418	360	(13.9)
Total operating revenues	4,638	4,807	3.6
Operating expenses:			
Operational and support expenses	2,168	2,439	12.5
Depreciation and amortization	962	1,014	5.4
Total Operating expenses	3,130	3,453	10.3
Operating income	1,508	1,354	(10.2)
Segment net income	$ 837	$ 766	(8.5)

Key Indicators			
Access line counts (000's):			
Access lines:			
Residential	17,205	16,915	(1.7)
Business	8,481	8,441	(0.5)
Other	256	218	(14.8)
Total access lines	25,942	25,574	(1.4)
Access line equivalents (1)	24,937	36,693	47.1
Total equivalent access lines	50,879	62,267	22.4
Resold lines and unbundled network elements (000's)	1,188	1,596	34.3
Access minutes of use (millions)	28,859	26,922	(6.7)
IntraLATA toll messages (millions)	125	109	(12.8)
Internet customers (000's)	871	1,141	31.0
ADSL customers (000's)	134	463	245.5
Digital and data services revenues	$860	$1,110	29.1
Calling feature revenues	$551	$580	5.3

	For the Nine Months Ended September 30,		%
	2000	2001	Change
Results of Operations			
Operating revenues:			
Local service	$8,607	$8,877	3.1
Network access	3,596	3,715	3.3
Long distance	517	539	4.3
Other communications	1,161	1,161	0.0
Total operating revenues	13,881	14,292	3.0

Operating expenses:			
Operational and support expenses	6,516	6,995	7.4
Depreciation and amortization	2,813	3,003	6.8
Total Operating expenses	9,329	9,998	7.2
Operating income	4,552	4,294	(5.7)
Segment net income	$2,540	$2,440	(3.9)

Key Indicators			
Access minutes of use (millions)	86,786	83,338	(4.0)
IntraLATA toll messages (millions)	390	331	(15.1)
Digital and data services revenues	$2,466	$3,171	28.6
Calling feature revenues	$1,598	$1,724	7.9

(1) Access line equivalents represent a conversion of non-switched data circuits to a switched access line basis and are presented for comparability purposes. Equivalents are calculated by converting high-speed/high-capacity data circuits to the equivalent of a switched access line based on transport capacity. While the revenues generated by access line equivalents have a directional relationship with these counts, growth rates cannot be compared on an equivalent basis.

Operating Revenues

Local service
The increase in local service revenues of $115 in the third quarter and $270 for the year-to-date period is attributable to strong growth in digital and data revenues, wholesale revenues, and by our marketing of calling features. Those increases were offset by a decrease in basic service revenues reflecting competition, rate reductions and a slowing economy as well as reduced payphone related revenues at our telephone operations.

Since third quarter 2000, residential access lines declined 1.7% to 16,915 and business access lines decreased 0.5% to 8,441. The core business was affected by a slowing economy, as well as competitive and technological changes. The technological changes are manifested in the shifting of customers from wireline to wireless and second line customers to high-speed access service. In addition, at September 30, 2001, we provided 1.6 million wholesale lines to competitors, on both a resale and unbundled network elements (UNE) basis. At September 30, 2000, UNEs accounted for approximately 33% of our wholesale lines and at September 30, 2001 they represented 57%. Because of the larger discounts associated with UNEs versus resale, this shift to UNEs is negatively impacting our revenue growth. We also estimate that we have lost an additional 1.9 million lines to facilities-based competitors.

Due to expanding demand for our digital and data services, we ended the third quarter with over 62 million total equivalent access lines, an increase of 22.4% since September 30, 2000.

Revenues from optional calling features such as Caller ID, Call Waiting, Call Return and voicemail service increased $29, or 5.3%, quarter over quarter and $126, or 7.9%, year over year. These increases were driven by growth in calling feature usage through our Complete Choice(R) Package, a one-price bundled offering of over 20 services.

Increased penetration of extended local area calling plans also increased local service revenues by approximately $11 compared to third quarter 2000 and $57 compared to the first nine months of 2000.

Network access

Network access revenues increased $98 in the third quarter of 2001 when compared to the same 2000 period, and $119 year over year. Revenues from dedicated high-capacity data line offerings grew approximately $108 quarter over quarter and $319 year over year as Internet service providers and high-capacity users increased their use of our network. The increases were offset by a $12 decline in the third quarter 2001 and a $210 decline for the year-to-date period in revenues derived from switched access services resulting from a decrease in access minutes-of-use volumes and the impacts of access charge rate reductions.

Access minutes of use fell 6.7% to 26,922 million in third quarter 2001 from 28,859 million in third quarter 2000. For the year-to-date period, access minutes of use decreased 4.0% to 83,338 million in 2001 from 86,786 million in 2000. These decreases resulted from: Continued migration of minutes to dedicated digital and data services offerings which are fixed-charge based rather than minute-of-use based; competition from competitive local exchange carriers whose traffic completely bypasses our network; and the effect of competitive services such as wireless and Internet e-mail.

The year-to-date period was negatively impacted by $50 of access charge rate reductions. These rate reductions are primarily related to the FCC's access reform and productivity factor adjustments. The reductions were partially offset by recoveries of local number portability costs. The quarter over quarter impact related to the rate reductions was insignificant.

Long distance

Long distance revenue increased $14 in the third quarter 2001 and $22 for the year-to-date period. Strong growth in wireless long distance and prepaid long distance cards was partially offset by losses in intralata toll as toll messages declined 12.8% for the quarter, and 15.1% year-to-date. These losses are driven by increased demand for Area Plus, a BellSouth package that combines a basic telephone line with an expanded local calling area. Area Plus packages grew 15.1% in the past year to over 2 million.

Other communications

Other communications revenue decreased $58 in the third quarter 2001 and remained flat for the year-to-date period. Two factors driving the decrease are a reduction in payphone revenues as BellSouth continues to transition out of this business by year-end 2003 and impacts related to exiting the wireless entertainment business.

Operating Expenses

Operational and support expenses

Operational and support expenses increased $271, quarter over quarter and $479 year over year. Included in these changes were expenses primarily attributable to labor costs to support data growth initiatives, customer service initiatives, wholesale long distance business and expenses related to information technology, which increased $151 for the third quarter 2001 and $500 for the year-to-date period. In addition, the provision for uncollectibles increased $43 for the quarter 2001 and $99 for the year-to-date period as the slowing economy caused an increase in CLEC and small business failures. The increases were offset by income generated as favorable pension plan returns exceeded expenses from other employee benefits.

Depreciation and amortization

Depreciation and amortization expense increased $52 in third quarter 2001 and $190 for the year-to-date period when compared to the same 2000 periods. The increases are primarily attributable to amortization of capitalized software and depreciation resulting from higher levels of net property, plant and equipment.

Domestic Wireless

During fourth quarter 2000, we contributed our domestic wireless operations to Cingular, and we account for our investment in Cingular under the equity method. For management purposes, however, we evaluate our domestic wireless segment based on our proportionate share of Cingular's results. Accordingly, the operating revenues and expenses reported for our domestic wireless segment for third quarter and year-to-date 2001 reflect 40% of Cingular's total revenues and expenses, whereas third quarter and year-to-date 2000 reflect the historical results of our wireless businesses that have been contributed to Cingular.

Certain reclassifications of prior period amounts have been made, where appropriate, to reflect comparable operating results.

	For the Three Months Ended September 30,		%
	2000	2001	Change
Total operating revenues	$1,071	$1,465	36.8
Operating expenses:			
Operational and support expenses	776	975	25.6
Depreciation and amortization	151	199	31.8
Total operating expenses	927	1,174	26.6
Operating income	144	291	102.1
Segment net income	$ 98	$ 128	30.6
Customers (a)	5,711	8,512	49.0
Average monthly revenue per customer (a)	$ 60	$ 53	(11.7)

	For the Nine Months Ended September 30,		%
	2000	2001	Change
Total operating revenues	$3,057	$4,189	37.0
Operating expenses:			
Operational and support expenses	2,226	2,821	26.7
Depreciation and amortization	472	569	20.6

Total operating expenses	2,698	3,390	25.6
Operating income	359	799	122.6
Segment net income	$ 245	$ 345	40.8
Average monthly revenue per customer (a)	$ 60	$ 52	(13.3)

(a) For third quarter and year-to-date 2000, the amounts shown are for our consolidated properties and do not include customer data for our unconsolidated properties. Customer data for the third quarter and year-to-date 2001 is comprised of BellSouth's 40% share of the managed results of Cingular Wireless.

Operating Revenues

Total operating revenues grew $394 for third quarter 2001 and $1,132 for the year-to-date period when compared to the same 2000 periods. These growth rates are attributable to higher airtime, access and equipment sales revenues driven by the higher customer base created by the formation of Cingular. Cingular's revenues increased 11.4% from proforma third quarter 2000 results and 13.1% from proforma year-to-date results, driven by a 12.8% increase in cellular and PCS customer levels.

We expect competition to continue to intensify and pressure pricing in our markets. We believe this will further stimulate customer growth and demand and continue to increase usage as the overall market is expanded.

Operating Expenses

Operational and support expenses

Operational and support expenses increased $199 during third quarter 2001 and $595 for the year-to-date period when compared to the same 2000 periods. These increases were also attributable to the change in operations between periods. Cingular's expenses increased 10.4% over proforma third quarter 2000 results and 13.4% over proforma year-to-date 2000 results. Cingular's pro forma expense growth was driven by increased service costs resulting from a rise in minutes of use, higher bad debt expense due to the slowing economy, higher cash expenses for marketing and advertising related to Cingular's national branding campaign and merger and integration related expenses.

Depreciation and amortization

Depreciation and amortization increased $48 during third quarter 2001 and $97 for the year-to-date period when compared to the same 2000 periods. Cingular's expenses increased 13.6% over proforma third quarter 2000 results and 5.2% over proforma year-to-date 2000 results, impacted by higher levels of gross property, plant and equipment.

Latin America Group

The Latin America group is comprised of our investments in wireless businesses in eleven countries in Latin America. Consolidated operations include our businesses in Argentina, Chile, Colombia, Ecuador, Nicaragua, Peru and Venezuela. All other businesses are accounted for under the equity method, and accordingly their results are reported as Net earnings (losses) of equity affiliates.

	For the Three Months Ended September 30,		%
	2000	2001	Change
Total operating revenues	$772	$716	(7.3)
Operating expenses:			
Operational and support expenses	581	492	(15.3)
Depreciation and amortization	167	138	(17.4)
Total operating expenses	748	630	(15.8)
Operating income	24	86	N/M*
Net earnings (losses) of equity affiliates	(19)	(50)	N/M
Segment net income (loss)	$(62)	$(52)	N/M
Customers (a)	6,668	8,092	21.4
Average monthly revenue per customer (a)	$31	$24	(22.6)

	For the Nine Months Ended September 30,		%
	2000	2001	Change
Total operating revenues	$2,171	$2,247	3.5
Operating expenses:			
Operational and support expenses	1,684	1,627	(3.4)
Depreciation and amortization	423	447	5.7
Total operating expenses	2,107	2,074	(1.6)
Operating income	64	173	N/M
Net earnings (losses) of equity affiliates	(61)	(187)	N/M
Segment net income (loss)	$(116)	$(277)	N/M
Average monthly revenue per customer (a)	$ 32	$ 26	(18.8)

* - Not Meaningful.

(a)......The amounts shown are for our consolidated properties and do not include customer data for our unconsolidated properties.

Operating Revenues

For the 2001 periods, segment revenues decreased $56 compared to third quarter 2000 and increased $76 on a year-to-date comparative basis. These changes were favorably affected by the addition of the Colombia operations, which increased $30 for the quarter and $182 for the year-to-date period. Adjusted for Colombia, revenues decreased $86 quarter over quarter and $106 year over year.

The decrease of $86 quarter over quarter and $106 year over year is due to a change in the interconnection agreements at our Venezuelan operations, which reduced revenues approximately $40 in the third quarter, and by a stronger U.S. Dollar against foreign currencies. Absent changes in foreign currency exchange rates, reported revenues would have increased an additional $46 for the quarter and an additional $110 for the year-to-date period.

Absent the impacts of the interconnection agreements and foreign currency losses, revenue growth for the quarter and the year remained relatively flat. Since September 30, 2000, our existing operations have added approximately 1.4 million customers, largely due to expansion in our Colombian and Venezuelan operations. However, offsetting the impacts of customer growth is declining monthly revenue per customer resulting from increased penetration of our cellular service into the mass-consumer market and exchange rate declines in some countries. Revenues were also negatively impacted by competitive and economic pressures on Listel, one of our advertising and publishing subsidiaries in Brazil.

Operating Expenses

Operational and support expenses
For the 2001 periods, these expenses decreased $89 compared to third quarter 2000 and $57 on a year-to-date comparative basis. The changes in both the quarter and year-to-date periods were favorably affected by reductions in expenses resulting from lower gross customer additions. The expense reductions were offset by increased expenses from the addition of the Colombian operations.

Operational and support expenses denominated in local currencies were favorably impacted by the weakening of foreign currencies against the U.S. Dollar. Absent changes in foreign currency exchange rates, reported operational and support expenses would have increased an additional $36 for the quarter and $74 for the year-to-date period.

Depreciation and amortization
Depreciation expense decreased $12 quarter over quarter and $6 year over year as a result of lower depreciation in Venezuela due to a change in the useful life of certain network equipment effective first quarter 2001 offset by higher gross depreciable plant resulting from the continued investment in our wireless network infrastructure. Amortization expense decreased $17 quarter over quarter. During the third quarter of 2001, we finalized the purchase price allocation of the Colombia acquisition, which resulted in a reclassification of intangibles and related reduction of amortization expense. Amortization expense increased $30 for the year-to-date period as a result of the addition and expansion of Colombia.

Net Earnings (Losses) of Equity Affiliates

Net earnings (losses) from our international equity affiliates decreased $31 to $(50) in third quarter 2001 and $126 to $(187) for the year-to-date period. The decline in earnings from our unconsolidated international businesses is due to lower operating results from our two principal investments in Brazil. Both of these businesses experienced significant foreign exchange losses as a result of the weakening of the Brazilian Real against the U.S. Dollar. A portion of our costs and expenses (e.g., handsets, depreciation and interest expense) is denominated in U.S. Dollars, while all of our revenues are denominated in Reals. In a period of devaluation, this relationship causes a negative impact on our margins. In addition, a substantial portion of our indebtedness is denominated in U.S. Dollars. As a result, the local currency balance of such debt increases to reflect the additional Reals required to meet such U.S. Dollar liabilities.

Third quarter and year-to-date foreign exchange losses in our Brazil equity investments decreased our net income by $47 and $163, respectively. In order to mitigate the risk of future foreign currency exchange losses, our Brazilian operations have recently increased the level of hedging activities to both lock in foreign exchange rates on known U.S. Dollar payments and to convert U.S. Dollar debt to local currency debt.

Domestic Advertising and Publishing

Our Domestic advertising and publishing segment is comprised of companies in the U.S. that publish, print, sell advertising in and perform related services concerning alphabetical and classified telephone directories and electronic product offerings.

	For the Three Months Ended September 30,		%
	2000	2001	Change
Total operating revenues	$545	$496	(9.0)
Operating expenses:			
Operational and support expenses	244	232	(4.9)
Depreciation and amortization	8	7	(12.5)
Total operating expenses	252	239	(5.2)
Operating income	293	257	(12.3)
Segment net income	$181	$158	(12.7)

	For the Nine Months Ended September 30,		%
	2000	2001	Change
Total operating revenues	$1,346	$1,376	2.2
Operating expenses:			
Operational and support expenses	672	677	0.7
Depreciation and amortization	22	20	(9.1)
Total operating expenses	694	697	0.4

Operating income	652	679	4.1
Segment net income	$399	$414	3.8

Operating Results

Revenues decreased $49 for third quarter 2001 and increased $30 for the year-to-date period when compared to the same 2000 periods. Operational and support expenses decreased $12 for third quarter 2001 and increased $5 for the year-to-date period when compared to the same 2000 periods. Revenues for third quarter were affected by book shifts, however year-to-date revenues were not impacted. Overall results were negatively impacted by a deterioration of economic conditions which have negatively impacted both revenue growth and bad debt expense.

All Other

This segment primarily includes our equity investments in wireless communications operations in Israel, Germany, Denmark and India. In addition, other minor revenue sources are included.

	For the Three Months Ended September 30,		%
	2000	2001	Change
Total operating revenues	$23	$35	52.2
Operating expenses	15	29	93.3
Operating income	8	6	N/M*
Net earnings (losses) of equity affiliates	(12)	14	N/M
Segment net income (loss)	$(10)	$18	N/M

	For the Nine Months Ended September 30,		%
	2000	2001	Change
Total operating revenues	$74	$102	37.8

Operating expenses	61	83	36.1
Operating income	13	19	N/M
Net earnings (losses) of equity affiliates	22	(15)	N/M
Segment net income (loss)	$23	$ (3)	N/M

* - Not Meaningful.

Operating Results

Revenues increased $12 for third quarter 2001 and $28 for the year-to-date period when compared to the same 2000 periods. Operating expenses increased $14 quarter over quarter and $22 year over year.

Net earnings (losses) from equity affiliates increased $26 quarter over quarter and decreased $37 year over year. The increase in the current quarter was driven primarily by our equity affiliate in Israel, while prior year quarter and current year-to-date losses are due to our equity affiliate in Germany.

Financial Condition

Cash flows from operations are our primary source of funding for capital requirements of existing operations, debt service and dividends. At September 30, 2001, our corporate debt rating was Aa3 by Moody's and A+ by S&P, which we believe gives us ready access to capital markets in the event additional funding is necessary. While current liabilities exceed current assets, our sources of funds -- primarily from operations and, to the extent necessary, from readily available external financing arrangements -- are sufficient to meet all current obligations on a timely basis. We believe that these sources of funds will be sufficient to meet the needs of our business for the foreseeable future.

Net cash provided by (used for):

	For the Nine Months Ended September 30,			
	2000	2001	Change	
Operating activities	$ 6,750	$ 6,361	$ (389)	(5.8)%
Investing activities	$ (7,150)	$ (5,384)	$ 1,766	(24.7)%
Financing activities	$ 289	$ (1,184)	$ (1,473)	N/M*

* - Not Meaningful.

Net cash provided by operating activities
The decrease in cash from operations between 2000 and 2001 primarily reflects traditional working capital requirements including supporting strategic initiatives on data. Year-to-date 2000 included operating cash flows of approximately $633 from our former domestic wireless operations, which were contributed to Cingular. This decrease was to some extent offset by favorable timing of tax and other payments supporting operational activity.

Net cash used in investing activities
During the first nine months of 2001, we invested $4,724 for capital

expenditures to support our wireline and wireless networks, to promote the introduction of new products and services and to increase operating efficiency and productivity. Significant investments are also being made to support deployment of high-speed Internet access and optical fiber-based broadband services. Also, during 2001 we invested approximately $130 into our wireless operations in Brazil and invested $279 in loan participation agreements related to our Colombian operations and advanced $1,382 to E-plus via a demand note replacing previously guaranteed debt. The first nine months of 2001 investing activities also include the receipt of approximately $1,100 from the sale of Qwest common stock.

Net cash used in financing activities

During the first nine months of 2001 we reduced our net commercial paper borrowings primarily with $1,100 of proceeds from the sale of Qwest common stock shares and $1,000 of proceeds from the private sale of debt securities. These reductions were substantially offset by new borrowings to fund advances to affiliates. During the first nine months of 2000, we issued $2,000 of long-term debt. The proceeds of $1,974 from this issuance were used to retire commercial paper borrowings.

Our debt to total capitalization ratio was 52.6% at September 30, 2001 compared to 54.2% at December 31, 2000. The change is primarily a function of decreases in short-term debt driven by reductions in commercial paper.

At October 31, 2001, we had a shelf registration statement on file with the SEC under which $2,250 of debt securities could be publicly offered.

Market Risk

For a complete discussion of our market risks, you should refer to the caption "Quantitative and Qualitative Disclosure About Market Risk" in our 2000 Annual Report on Form 10-K. Our primary exposure to market risks relates to unfavorable movements in interest rates and foreign currency exchange rates. We do not anticipate any significant changes in our objectives and strategies with respect to managing such exposures.

During the third quarter 2001, our equity investees in Brazil increased hedging activity to reduce exposure to foreign currency risk. See discussion in Latin America group segment.

Operating Environment and Trends of the Business

Regulatory Developments

Our future operations and financial results will be substantially influenced by developments in a number of federal and state regulatory proceedings. Adverse results in these proceedings could materially affect our revenues, expenses and ability to compete effectively against other telecommunications carriers.

Federal policies implemented by the Federal Communications Commission (FCC) have strongly favored access reform, whereby the historical subsidy for local service that is contained in network access charges paid by long distance carriers is moved to end-user charges or universal service funds, or both. On April 27, 2001, the FCC released a Notice of Proposed Rulemaking that commences a broad inquiry that will begin a fundamental examination of all forms of inter-carrier compensation--payments among telecommunications carriers resulting from their interconnecting networks. In general, there are two broad classes of intercarrier compensation: (1) reciprocal compensation that applies to local calls; and (2) access charges that apply to long distance calls. The objective of the Notice of Proposed Rulemaking is to examine the existing rules pertaining to inter-carrier compensation and explore alternative forms of inter-carrier compensation. This proceeding could lead to permanent changes in the compensation that BellSouth currently receives from other carriers and its end user customers. One alternative under consideration is "bill and keep," a policy that requires carriers to exchange traffic freely with each other and to recover from end user customers the costs of originating and terminating traffic. In addition, there are other aspects of access charges and universal service fund contribution requirements that continue to be considered by the state and federal regulatory commissions that could result in greater expense levels or reduced revenues.

The FCC has considerable authority to establish pricing, interconnection and other policies that had once been considered within the exclusive jurisdiction of the state public service commissions. We expect the FCC to continue policies that promote local service competition.

In 1997 and 1998, we petitioned the FCC for permission under the Telecommunications Act of 1996 to offer full long distance services in South Carolina and Louisiana. The FCC has denied these petitions. In October 2001, after unanimous endorsements by the Georgia and Louisiana Public Service Commissions, we filed applications with the FCC for long distance authority for those two states. In October 2001, the Mississippi Public Service Commission unanimously endorsed our seeking long distance relief in that state. We have also made filings with the public service commissions in each of Alabama, Florida, Kentucky, North Carolina, South Carolina and Tennessee to review our compliance with the requirements for obtaining long distance authority. We expect to file an application with the FCC for each state at the appropriate point in the state commission's consideration. We do not know if the FCC will require further changes in our network interconnection elements and operating systems before it will approve such petitions. These changes could result in significant additional expenses and increase local service competition from CLEC's that use our network.

On April 27, 2001, the FCC released an Order on Remand and Report and Order addressing the issue of compensation for ISP traffic. In its Order, the FCC acknowledged that dial-up calls to Internet service providers are not local calls, but instead are "information access" traffic exempt from the reciprocal compensation provisions of the 1996 Act. The FCC has implemented a three-year interim period during which local carriers will pay inter-carrier compensation for such calls in decreasing increments. After the three-year interim period, the new rules on inter-carrier compensation to be adopted in connection with the Notice of Proposed Rulemaking referred to above are expected to be in effect. If no rules have been adopted by that time, the inter-carrier compensation in effect at the end of the third year would remain in effect.

Our intrastate prices are regulated under price regulation plans provided by statute or approved by state public service commissions. Some plans are subject to periodic review and may require renewal. The commissions reviewing these plans may require price reductions and other concessions from us as conditions to approving these plans.

The Mississippi Public Service Commission has completed its review of the Mississippi price regulation plan. In this order dated October 31, 2001, the Mississippi Commission approved the plan for an additional six year term with certain modifications, including new performance measures. As a part of the renewal and review process, the Mississippi Commission could require modifications to prices and other terms of the plan.

In January 2001, the Georgia Public Service Commission entered an order adopting new company performance measures, which will be used as one means to assess our wholesale service quality to competitive local exchange carriers. In addition, the Commission adopted an Enforcement Plan. The Enforcement Plan consists of three tiers. Under tier 1, we will be required to pay remedial sums to individual competitive local exchange carriers if we fail to meet certain performance criteria set by the Commission. Under tier 2, we will pay additional sums directly to the State Treasury for failing to meet certain performance metrics. Under tier 3, if we fail to meet certain performance criteria, then we will suspend additional marketing and sales of long distance services allowed by the Telecommunications Act of 1996. Our annual liability under the Plan will be capped at 44% of net revenues in Georgia. The decision also adopts other remedial measures for the filing of late or incomplete performance reports, and a market penetration adjustment for new and advanced services, which increases the amount of the payments where low volumes of advanced or nascent services are involved. The Enforcement Plan went into effect on March 1, 2001. We have made payments under the Enforcement Plan and we may be required to make payments in the future.

In May 2001, the Louisiana Public Service Commission issued an order adopting new company performance measures, in addition to clarification of existing measures, which will be used as one means to assess our wholesale service quality to competitive local exchange carriers. In addition, the Commission adopted an Enforcement Plan. The Enforcement Plan consists of three tiers. Under tier 1, we will be required to pay remedial sums to individual competitive local exchange carriers if we fail to meet certain performance criteria set by the Commission. Under tier 2, we will pay additional sums directly to the State Treasury for failing to meet certain performance metrics. Under tier 3, if we fail to meet certain performance criteria, then the Louisiana Public Service Commission may initiate a proceeding to determine whether to recommend to the FCC suspension of our marketing and sales of long distance services allowed by the Telecommunications Act of 1996. Our annual liability under the Plan will be capped at $59 in Louisiana. The order also adopts other remedial measures for the filing of late or incomplete performance reports, and a market penetration adjustment for new and advanced services, which increases the amount of the payments where low volumes of advanced or nascent services are involved. We have made payments under the Enforcement Plan and we may be required to make payments in the future.

In 2000, the Florida Public Service Commission commenced a proceeding to determine whether we violated certain Commission rules regarding service quality. This matter has been resolved with the adoption of a new service guaranty plan and the payment of monies to a fund promoting access to telecommunication services by people with low income. Also in 2000, the Commission issued a proposed agency action stating that our change in 1999 from a late charge based on a percentage of the amounts overdue to a flat rate fee plus an interest charge violated the Florida price regulation statute and voted that approximately $65 should be refunded. We protested the decision. On August 30, 2001, the Commission issued an order adopting its proposed action. We have appealed to the Florida Supreme Court and continue to collect the charges subject to refund.

We are involved in numerous legal proceedings associated with state and federal regulatory matters, the disposition of which could materially impact our operating results and prospects. See note N to our consolidated interim financial statements.

International Operations

Our reporting currency is the U.S. Dollar. However, most of our revenues are generated in the currencies of the countries in which we operate. In addition, many of our operations and equity investees hold U.S. Dollar-denominated short- and long-term debt. The currencies of many Latin American countries have experienced substantial volatility and depreciation in the past. Declines in the value of the local currencies in which we are paid relative to the U.S. Dollar will cause revenues in U.S. Dollar terms to decrease and dollar-denominated liabilities to increase. Where we consider it to be economically feasible, we attempt to limit our exposure to exchange rate fluctuations by using foreign currency forward exchange contracts or similar instruments as a vehicle for hedging; however, a substantial amount of our exposures are unhedged.

The impact of a devaluation or depreciating currency on an entity depends on the residual effect on the local economy and the ability of an entity to raise prices and/or reduce expenses. Our ability to raise prices is limited in many instances by government regulation of tariff rates and competitive constraints. Due to our constantly changing currency exposure and the potential substantial volatility of currency exchange rates, we cannot predict the effect of exchange rate fluctuations on our business.

Economic, social and political conditions in Latin America are, in some countries, unfavorable and volatile, which may impair our operations. These conditions could make it difficult for us to continue development of our business, generate revenues or achieve or sustain profitability. Historically, recessions and volatility have been primarily caused by: mismanagement of monetary, exchange rate and/or fiscal policies; currency devaluations; significant governmental influence over many aspects of local economies; political and economic instability; unexpected changes in regulatory requirements; social unrest or violence; slow or negative economic growth; imposition of trade barriers; and wage and price controls.

Most or all of these factors have occurred at various times in the last two decades in our core Latin American markets. We have no control over these matters. Economic conditions in Latin America are generally less attractive than those in the U.S., and poor social, political and economic conditions may inhibit use of our services which may adversely impact our business.

Cingular

In October 2001, Cingular entered into a joint venture with VoiceStream which enables Cingular to accelerate time-to-market in New York City. This agreement allows Cingular to share 40mhz of spectrum in New York and California. Also during 2001, Cingular, through an 85% non-controlling equity interest in Salmon PCS, was the bidding winner of 79 licenses in total including 30 licenses previously owned by NextWave. The total amount owed by Salmon related to these winning bids is approximately $2,300, which includes a previous deposit of $470.

New Accounting Pronouncements

See note B to our consolidated interim financial statements.

Item 3. QUALITATIVE AND QUANTITATIVE DISCLOSURES ABOUT MARKET RISK

See the caption labeled "Market Risk" in Management's Discussion and Analysis of Financial Condition and Results of Operations.

Cautionary Language Concerning Forward-Looking Statements

In addition to historical information, this document contains forward-looking statements regarding events and financial trends that may affect our future operating results, financial position and cash flows. These statements are based on our assumptions and estimates and are subject to risks and uncertainties. For these statements, we claim the protection of the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995.

There are possible developments that could cause our actual results to differ materially from those forecast or implied in the forward-looking statements. You are cautioned not to place undue reliance on these forward-looking statements, which are current only as of the date of this filing. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

While the below list of cautionary statements is not exhaustive, some factors that could affect future operating results, financial position and cash flows and could cause actual results to differ materially from those expressed in the forward-looking statements are:

- a change in economic conditions in domestic or international markets where we operate or have material investments which would affect demand for our services;
- significant deterioration in foreign currencies relative to the U.S. Dollar in foreign countries in which we operate;
- changes in U.S. or foreign laws or regulations, or in their interpretations, which could result in the loss, or reduction in value, of our licenses, concessions or markets, or in an increase in competition, compliance costs or capital expenditures;
- a decrease in the growth rate of demand for the services which we offer;
- the intensity of competitive activity and its resulting impact on pricing strategies and new product offerings;
- protracted delay in our entry into the interLATA long distance market;
- higher than anticipated start-up costs or significant up-front investments associated with new business initiatives;
- the outcome of pending litigation;
- unanticipated higher capital spending from, or delays in, the deployment of new technologies;
- the impact of terrorist attacks on our business;
- the impact and the success of the wireless joint venture with SBC Communications, known as Cingular Wireless, including marketing and product development efforts and financial capacity.

PART II -- OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits:

Exhibit Number	
4a	No instrument which defines the rights of holders of our long- and intermediate-term debt is filed herewith pursuant to Regulation S-K, Item 601(b)(4)(iii)(A). Pursuant to this regulation, we agree to furnish a copy of any such instrument to the SEC upon request.
10q-12	Amendment dated September 15, 2001 to the BellSouth Personal Retirement Account Pension Plan.
10z	BellSouth Compensation Deferral Plan as amended and restated effective January 1, 2002.
10jj	BellSouth Officer Compensation Deferral Plan.
11	Computation of Earnings Per Common Share.
12	Computation of Ratio of Earnings to Fixed Charges.

(b) Reports on Form 8-K:

Date of Event	Subject
July 10, 2001	Reciprocal Compensation Accrual Adjustment
July 23, 2001	BellSouth 2Q01 Earnings Release

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

BELLSOUTH CORPORATION

By /s/ W. Patrick Shannon

W. PATRICK SHANNON
Vice President - Finance and Supply Chain Management
(Principal Accounting Officer)

November 5, 2001

EXHIBIT INDEX

Exhibit Number	
10q-12	Amendment dated September 15, 2001 to the BellSouth Personal Retirement Account Pension Plan.
10z	BellSouth Compensation Deferral Plan as amended and restated effective January 1, 2002.
10jj	BellSouth Officer Compensation Deferral Plan.
11	Computation of Earnings Per Common Share.
12	Computation of Ratio of Earnings to Fixed Charges.