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DOCKET NO.

Public Utilities Commission of the State of South Dakota

DATE	MEMORANDA
11/23/99	Filed and Docketed;
11/24/99	Weekly Filing;
12/17/99	Revised Brief;
1/12/00	Order Granting COA;
1/12/00	Docket Closed.

TC99-108

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November 22, 1999

VIA OVERNIGHT DELIVERY

William Bullard, Executive Director
South Dakota Public Utilities Commission
500 E. Capitol Ave.
State Capitol Building, First Floor
Pierre, South Dakota 57501

RECEIVED
NOV 23 1999
SOUTH DAKOTA PUBLIC
UTILITIES COMMISSION

Re: Application of NetLojix Telecom, Inc.

Dear Mr. Bullard:

Enclosed for filing on behalf of NetLojix Telecom, Inc. ("NetLojix") are an original and ten (10) copies of NetLojix's Application for a Certificate of Authority to Provide Resold Interexchange Telecommunications Services in South Dakota ("Application"). A check for \$250.00 is also enclosed to cover the requisite filing fee.

Please date-stamp the enclosed extra copy of this letter and return it in the self-addressed, postage-paid envelope attached. Should you have any questions concerning this filing, please do not hesitate to contact the undersigned.

Respectfully submitted,



Kemal M. Hawa
Paul W. Garnett

Counsel for NetLojix Telecom, Inc.

Enclosures

cc: Craig Clark
Ernest Gillespie
Russell Blau (w/o encl.)
Brett Ferenchak (w/o encl.)
Megan Rha (w/o encl.)

**BEFORE THE
SOUTH DAKOTA PUBLIC UTILITIES COMMISSION**

Application of	)	
	)	
NetLojix Telecom, Inc.	)	
	)	Docket No. _____
For a Certificate of Authority to Provide	)	
Resold Interexchange Telecommunications	)	
Services within the State of South Dakota	)	

APPLICATION FOR CERTIFICATE OF AUTHORITY

NetLojix Telecom, Inc. ("NetLojix" or "Applicant"), by its undersigned counsel, hereby submits its Application for a Certificate of Authority to provide resold intrastate interexchange telecommunications services pursuant to Section 49-31-3 of the South Dakota Administrative Rules and the Rules of the Public Utilities Commission.

In support of this Application, pursuant to Section 20:10:24:02 of the Telecommunications Service Rules, NetLojix provides the following information:

1. 20:10:24:02(1). Name, address, and telephone number of applicant. Applicant's legal name is NetLojix Telecom, Inc. Applicant maintains its principal place of business at:

501 Bath Street
Santa Barbara, CA 93101
Telephone: (805) 884-6300
Facsimile: (805) 884-6311

Correspondence or communications pertaining to this Application should be directed to Applicant's attorneys of record:

Kemal M. Hawa, Esq.
Paul W. Garnett, Esq.
Swidler Berlin Shereff Friedman, LLP
3000 K St., N.W., Suite 300
Washington, D.C. 20007-5116
Telephone: (202) 424-7500
Facsimile: (202) 424-7645

with a copy to:

Michael D. Ussery
Chief Financial Officer and Chief Accounting Officer
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180
Telephone: (817) 788-3077
Facsimile: (817) 788-3355

2. 20:10:24:02(2). Name under which applicant will provide services. Applicant will provide the proposed services under the name of "NetLojix Telecom, Inc."

3. 20:10:24:02(3). Legal organization.

a. 20:10:24:02(3)(a). State of organization, date of organization, and authority to transact business in South Dakota. Applicant is a corporation organized under the laws of Delaware on August 25, 1999, and is qualified to do business in South Dakota. A copy of Applicant's Certificate of Incorporation and a copy of its certificate of authority to transact business in South Dakota are included as Exhibit 1.

b. 20:10:24:02(3)(b). Location of principal office in South Dakota and registered agent. Applicant does not currently have an office within South Dakota. NetLojix's registered agent in South Dakota is:

CT Corporation System
319 S. Coteau Street
Pierre, SD 57501

c. 20:10:24:02(3)(c). Ownership and management interest. NetLojix is a wholly owned subsidiary of NetLojix Communications, Inc.^{1/}, a publicly traded Delaware corporation.

Applicant's officers and directors are as follows:

Anthony E. Papa
James P. Pisani
Michael D. Ussery

Chairman of the Board and Chief Executive officer
President
Chief Financial Officer and Chief Accounting Officer

All officers can be reached at the following address:

NetLojix Telecom, Inc.
501 Bath Street
Santa Barbara, CA 93101
Telephone: (805) 884-6300
Facsimile: (805) 884-6311

NetLojix's management personnel are well qualified to execute its business plan, having extensive managerial and technical telecommunications experience. Descriptions of the telecommunications and managerial experience of Applicant's key personnel are attached hereto as Exhibit 2.

4. 20:10:24:02(4). Partnership information. Applicant is not a partnership.

^{1/} NetLojix Communications Inc. was originally named AvTel Communications, Inc. The name change took effect September 15, 1999.

5. 20:10:24:02(5). Proposed services. Applicant proposes to provide resold intrastate interexchange telecommunications services to and from all points within the State of South Dakota. Applicant's services will be available on a full-time basis, twenty-four (24) hours a day, seven (7) days a week. Applicant proposes initially to provide resold intrastate interexchange telecommunications services, including direct dialed 1 + service, inbound/outbound message telecommunications service, switched and dedicated services, toll free service and post-paid calling service to and from all points within the State of South Dakota.

6. 20:10:24:02(6). Facilities to be used to provide services. As a resale carrier, Applicant has not installed nor does it currently plan to install any equipment, plant, or facilities in the State of South Dakota. In South Dakota, NetLojix will resell the facilities-based interexchange services of certified carriers, such as Sprint, IXC or DCA. In the event NetLojix subsequently formulates plans for installing any facilities in South Dakota, it will notify the Commission and comply with all regulations, as appropriate.

7. 20:10:24:02(7). Geographic area to be served. Applicant plans to provide resold interexchange telecommunications services to subscribers to and from all points in South Dakota, and, therefore, seeks statewide authorization. Since NetLojix seeks to provide statewide authority, Applicant has not included a map showing proposed service areas.

8. 20:10:24:02(8). Financial qualifications and tariff. NetLojix has access to the financing and capital necessary to conduct the telecommunications operations as specified in this Application. As a wholly owned subsidiary of NetLojix Communications, Inc. ("NetLojix Communications"), NetLojix will rely upon the substantial financial resources of its corporate parent. Therefore, NetLojix submits as Exhibit 3 the financial statements of its corporate parent,

NetLojix Communications. For the year ending December 31, 1998, NetLojix Communications had total assets of \$16 million, which exceeded total liabilities of \$11.5 million, providing stockholders' equity of \$4.5 million. With access to the substantial financial resources of its parent, NetLojix Communications, NetLojix is financially well qualified to provide the telecommunications services proposed in this Application.

A copy of NetLojix's proposed tariff containing NetLojix's rates and terms and conditions of service is attached hereto as Exhibit 4.

9. 20:10:24:02(9). Complaint contact, regulatory contact, and handling of billing and customer service matters. All inquiries regarding complaints and regulatory, billing and consumer services matter should be referred to:

Michael D. Ussery
Chief Financial Officer and Chief Accounting Officer
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180
Telephone: (817) 788-3077
Facsimile: (817) 788-3355

Questions concerning the ongoing operations of NetLojix following certification should be directed to Mr. Ussery at the above address.

Customers with service, billing and repair questions or complaints may reach NetLojix at its 24-hour toll-free customer service number, 1-877-NETLOJIX, for assistance. In the event of a billing dispute, NetLojix will perform a review of the disputed billing amount and attempt to reach a settlement to the mutual satisfaction of both parties. Following a full investigation to determine whether or not the charges are improper, NetLojix may adjust the disputed bill.

10. 20:10:24:02(10). Current authority to provide service. NetLojix is in the process of applying for authorization, where required, to provide intrastate interexchange services nationwide. NetLojix has not been denied authorization to provide service in any state and is in good standing in every state where it holds such authorization.

11. 20:10:24:02(11) Marketing. NetLojix intends to market its services to business customers in the State of South Dakota. NetLojix has not yet established specific marketing plans. NetLojix will comply with South Dakota law and the Federal Communications Commission's ("FCC") regulations governing changing a customer's primary interexchange carrier.

12. 20:10:24:02(12). Cost support. The services that NetLojix has proposed herein are competitive services; therefore, NetLojix has not provided cost support for the rates shown in its tariff.

13. 20:10:24:02(13). Federal tax identification number. Applicant's federal tax identification number is 87-0378021.

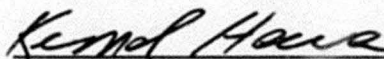
14. 20:10:24:02(14). Slamming and cramming complaints. There are no complaints against Applicant in any jurisdiction regarding the unauthorized switching of a customer's telecommunications provider or the act of charging customers for services that have not been ordered.

15. 20:10:24:02(16). Other information. The entry of NetLojix into the telecommunications business in South Dakota will serve the public interest by creating greater competition in the interexchange marketplace and permitting customers to achieve increased efficiencies and cost savings. NetLojix's proposed intrastate services will enhance the services available to consumers and increase consumer choice through innovative, diversified, and reliable service offerings.

Consumers will benefit both directly as a result of the competitively priced service options available from NetLojix and also indirectly as NetLojix's presence increases the incentives for other telecommunications providers to operate more efficiently, reduce prices, and offer more innovative services. Approval of this Application, therefore, will serve the public interest.

WHEREFORE, NetLojix Telecom, Inc. requests that the South Dakota Public Utilities Commission grant the requested Application authorizing it to provide intrastate interexchange telecommunications services in the State of South Dakota.

Respectfully submitted,



Kemal M. Hawa, Esq.

Paul W. Garnett, Esq.

SWIDLER BERLIN SHEREFF FRIEDMAN, LLP

3000 K St., N.W., Suite 300

Washington, D.C. 20007-5116

Telephone: (202) 424-7500

Facsimile: (202) 424-7645

Counsel for
NetLojix Telecom, Inc.

Dated: November 22, 1999

LIST OF EXHIBITS

EXHIBIT 1	Certificate of Incorporation and Certificate of Authority to Transact Business
EXHIBIT 2	Management Qualifications
EXHIBIT 3	Financial Statements of Applicant's Parent, NetLojix Communications, Inc.
EXHIBIT 4	Proposed Tariff
VERIFICATION	

EXHIBIT 1

**Certificate of Incorporation and
Certificate of Authority to Transact Business As a Foreign Corporation**

State of Delaware
Office of the Secretary of State

PAGE 1

I, EDWARD J. FREEL, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY THE ATTACHED IS A TRUE AND CORRECT COPY OF THE CERTIFICATE OF INCORPORATION OF "NETLOJIX TELECOM, INC.", FILED IN THIS OFFICE ON THE TWENTY-FIFTH DAY OF AUGUST, A.D. 1999, AT 6 O'CLOCK P.M.

A FILED COPY OF THIS CERTIFICATE HAS BEEN FORWARDED TO THE NEW CASTLE COUNTY RECORDER OF DEEDS.



Edward J. Freel, Secretary of State

3088370 8100

991356615

AUTHENTICATION:

DATE:

9940650

08-26-99

CERTIFICATE OF INCORPORATION**OF****NETLOJIX TELECOM, INC.****ARTICLE I.**

The name of the Corporation is **NETLOJIX TELECOM, INC.**

ARTICLE II.

The address of the Corporation's registered office in the State of Delaware is 1209 Orange Street, City of Wilmington, County of New Castle, Delaware 19805. The name of its registered agent at such address is The Corporation Trust Company.

ARTICLE III.

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

ARTICLE IV.

The Corporation is authorized to issue one class of stock, designated Common Stock. The number of shares of Common Stock authorized to be issued is 1,000 shares, par value \$0.001.

ARTICLE V.

The name and mailing address of the Incorporator is:

Janis St. Marie
c/o Seed, Mackall & Cole LLP
1332 Anacapa Street, Suite 200
Santa Barbara, California 93101

ARTICLE VI.

The Board of Directors of the Corporation is expressly authorized to make, alter, repeal, amend and rescind any or all of the Bylaws of the Corporation; to fix the amount to be reserved as working capital, and to authorize and cause to be executed, mortgages and liens without limit as to the amount, upon the property and franchise of this Corporation.

With the consent in writing, and pursuant to a vote of the holders of a majority of the capital stock issued and outstanding, the directors shall have authority to dispose, in any manner, of the whole property of this Corporation.

The Bylaws shall determine whether and to what extent the accounts and books of this Corporation, or any of them, shall be open to the inspection of the stockholders, and no stockholders shall have any right of inspecting any account, or book, or document of this Corporation, except as conferred by the law or the Bylaws, or by resolution of the stockholders.

The stockholders and directors shall have power to hold their meetings and keep the books, documents and papers of the Corporation outside of the State of Delaware, at such places as may be from time to time designated by the Bylaws or by resolution of the stockholders or directors, except as otherwise required by the laws of Delaware.

It is the intention that the objects, purposes and powers specified in the third paragraph hereof shall, except where otherwise specified in such paragraph, be nowise limited or restricted by reference to or inference from the terms of any other clause or paragraph in this Certificate of Incorporation, but that the objects, purposes and powers specified in the third paragraph and in each of the Articles or paragraphs of this charter shall be regarded as independent objects, purposes and powers.

ARTICLE VII.

A director of the Corporation shall not be personally liable to the Corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, except for liability (i) for any breach of the director's duty of loyalty to the Corporation or its stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) under Section 174 of the Delaware General Corporation Law, or (iv) for any transaction from which the director derived any improper personal benefit. If the Delaware General Corporation Law is amended after the filing of this Certificate of Incorporation to authorize corporate action further eliminating or limiting the personal liability of directors then the liability of a director of the Corporation shall be eliminated or limited to the fullest extent permitted by the Delaware General Corporation Law as so amended.

Any repeal or modification of the foregoing provisions of this Article VII by the stockholders of the Corporation shall not adversely affect any right or protection of a director of the Corporation existing at the time of such repeal or modification.

IN WITNESS WHEREOF, I have hereunto set my hand on this 25th of August, 1999


J. St. Marie, Incorporator

State of South Dakota



OFFICE OF THE SECRETARY OF STATE

Certificate of Authority

I, **JOYCE HAZELTINE**, Secretary of State of the State of South Dakota, hereby certify that the Application for a Certificate of Authority of **NETLOJIX TELECOM, INC. (DE)** to transact business in this state duly signed and verified pursuant to the provisions of the South Dakota Corporation Acts, have been received in this office and are found to conform to law.

ACCORDINGLY and by virtue of the authority vested in me by law, I hereby issue this Certificate of Authority and attach hereto a duplicate of the application to transact business in this state.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed the Great Seal of the State of South Dakota, at Pierre, the Capital, this November 3, 1999.



A handwritten signature in cursive script, reading "Joyce Hazeltine".

Joyce Hazeltine
Secretary of State

SECRETARY OF STATE
STATE CAPITOL
500 E. CAPITOL
PIERRE, S.D. 57501-5077
605-773-4845
FAX (605) 773-4550

FILE NO _____
RECEIPT NO _____ **RECEIVED**

NOV 03 1999

APPLICATION FOR CERTIFICATE OF AUTHORITY

Pursuant to the provisions of SDCL 47-8-7, the undersigned corporation hereby applies for a Certificate of Authority to transact business in the State of South Dakota and for that purpose submits the following statement:

(1) The name of the corporation is Netlojix Telecom, Inc.
(Exact corporate name)

(2) If the name of the corporation does not contain the word "corporation", "company", "incorporated" or "limited" or does not contain an abbreviation of one of such words, then the name of the corporation with the word or abbreviation which it elects to add thereto for use in this state is

(3) State where incorporated Delaware Federal Taxpayer ID# 77-0521934

(4) The date of its incorporation is August 25, 1999 and the period of its duration, which may be perpetual, is Perpetual

(5) The address of its principal office in the state or country under the laws of which it is incorporated is

1209 Orange Street, Wilmington, Delaware Zip Code 19801

mailing address if different from above is: Same

Zip Code _____

(6) The street address, or a statement that there is no street address, of its proposed registered office in the State of South Dakota is c/o C T Corporation System, 319 S. Coteau Zip 57501

and the name of its proposed registered agent in the State of South Dakota at that address is

C T Corporation System

(7) The purposes which it proposes to pursue in the transaction of business in the State of South Dakota are: (state specific purpose) provision of telecommunications services

(8) The names and respective addresses of its directors and officers are:

Name	Officer Title	Street Address	City	State	Zip
<u>Anthony E. Papa</u>	<u>Chief Executive Officer and</u>	<u>501 Bath Street, Santa Barbara, California</u>			<u>93101</u>
<u>James P. Pisani</u>	<u>President/Secretary and</u>	<u>501 Bath Street, Santa Barbara, California</u>			<u>93101</u>
<u>Michael D. Ussery</u>	<u>CFO/Chief Acct. Officer</u>	<u>8721 Airport Freeway, Fort Worth, Texas</u>			<u>76180</u>
_____	_____	_____	_____	_____	_____
_____	_____	_____	_____	_____	_____

(9) The aggregate number of shares which it has authority to issue, itemized by classes, par value of shares, shares without par value, and series, if any, within a class is:

Number of shares	Class	Series	Par value per share or statement that shares are without par value
<u>1,000</u>	<u>Common Stock</u>	<u>(No series)</u>	<u>\$0.01</u>

(10) The aggregate number of its issued shares, itemized by classes, par value of shares, shares without par value, and series, if any, within a class, is:

Number of shares	Class	Series	Par value per share or statement that shares are without par value
<u>100</u>	<u>Common Stock</u>	<u>(No series)</u>	<u>\$0.01</u>
_____	_____	_____	_____
_____	_____	_____	_____

(11) The amount of its stated capital is \$1.00

Shares issued times par value equals stated capital. In the case of no par value stock, stated capital is the consideration received for the issued shares.

(12) This application is accompanied by a CERTIFICATE OF FACT or a CERTIFICATE OF GOOD STANDING duly acknowledged by the secretary of state or other officer having custody of corporate records in the state or country under whose laws it is incorporated.

(13) That such corporation shall not directly or indirectly combine or make any contract with any incorporated company, foreign or domestic, through their stockholders or the trustees or assigns of such stockholders, or with any copartnership or association of persons, or in any manner whatever to fix the prices, limit the production or regulate the transportation of any product or commodity so as to prevent competition in such prices, production or transportation or to establish excessive prices therefor.

(14) That such corporation, as a consideration of its being permitted to begin or continue doing business within the State of South Dakota, will comply with all the laws of the said State with regard to foreign corporations.

The application must be signed, in the presence of a notary public, by the chairman of the board of directors, or by the president or by another officer.

I DECLARE AND AFFIRM UNDER THE PENALTY OF PERJURY THAT THIS APPLICATION IS IN ALL THINGS, TRUE AND CORRECT.

Dated Sept. 28 19 99

[Signature]
(Signature)

President
(Title)

State of California

County of Santa Barbara

On this 28th day of Sept. 19 99, before me Julie A. Brown
personally appeared James P. Pisani, known to me, or proved to me, to be
the President of the corporation that is described in and that executed the
within instrument and acknowledged to me that such corporation executed same.

My Commission Expires: 7/26/2001

Julie A. Brown
(Notary Public)

Notarial Seal



The Consent of Appointment below must be signed by the registered agent listed in number six.

CONSENT OF APPOINTMENT BY THE REGISTERED AGENT

I, C T Corporation System, hereby give my consent to serve as the
(name of registered agent)

registered agent for Netlojix Telecom, Inc.
(corporate name)

Dated 11-2 19 99

By: [Signature]
(signature of registered agent)

ASSISTANT VICE PRESIDENT

EXHIBIT 2

Management Qualifications

Managerial and Technical Qualifications of Key Personnel for Applicant

Anthony E. Papa has been the **Chairman of the Board and Chief Executive Officer of the Company** since October 1996. Mr. Papa was also President of the Company from October 1996 until February 1998. Prior to October, 1996, Mr. Papa had served as President of ICS Communications, Inc. ("ICS"), Richardson, Texas, a national provider of cable television, wireless paging, local and long distance telephone services from December 1992. Before joining ICS, Mr. Papa served as general manager for Spectradyn, Inc., the largest provider of pay-per-view entertainment and interactive services to the hospitality industry. Mr. Papa is a director of International School of Information Management, Inc., an accredited university and an electronic publisher and provider of electronic services, and a director of ABS-Clio, Inc., an international publisher of historical reference materials for institutions of higher education. Mr. Papa received a B.S. in Management from Iona College, in New Rochelle, New York.

James P. Pisani has been the **President** of the Company since February 1998, and has served as Chief Operating Officer, Chief Financial Officer and Secretary of the company since October 1996. Mr. Pisani has also served as Chief Accounting Officer of the Company since October 1998. From October 1996 to February 1998, Mr. Pisani was the Executive Vice President of the Company. Prior to October 1996, he served as Vice President of Sales and National Accounts for ICS. While at ICS, Mr. Pisani was responsible for that firm's business-to-business and consumer sales activities. Prior to joining ICS, from June 1989 to June 1994, Mr. Pisani served as Vice President of a national mortgage banking firm serving, primarily, institutional accounts. Mr. Pisani graduated from Princeton University in 1986, with a degree in Economics.

Michael D. Ussery is the **Chief Financial Officer and Chief Accounting Officer**. As the C.F.O. and the C.A.O. of NetLojix Telecom, Inc., Mr. Ussery is responsible for the preparation of financial statements, cash management and regulatory compliance of the company. Mr. Ussery has been a Certified Public Accountant since 1986. He has also worked in public accounting since 1981. Mr. Ussery is a member of the AICPA and FEI. He has written for and lectured to Certified Public Accountant groups on various accounting topics, including SEC reporting, foreign GAAP and accounting principles.

EXHIBIT 3

Financial Statements of Applicant's Parent, NetLojix Communications, Inc.

Attached as Exhibit 3 are the financial statements of NetLojix Communications, Inc., the corporate parent of NetLojix Telecom, Inc. As explained in Footnote 1, NetLojix Communications, Inc. changed its name from AvTel Communications, Inc.

INDEPENDENT AUDITORS' REPORT

The Board of Directors
AVTel Communications, Inc.:

We have audited the accompanying consolidated balance sheets of AVTel Communications, Inc. and subsidiaries as of December 31, 1998 and 1997, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 1998. In connection with our audits of the consolidated financial statements, we also have audited the accompanying financial statement schedule. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of AVTel Communications, Inc. and subsidiaries at December 31, 1998 and 1997, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 1998, in conformity with generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

KPMG LLP

Dallas, Texas
April 14, 1999

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS

December 31, 1998 and 1997

	1998	1997
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 911,179	4,807,441
Accounts receivable, net	4,804,532	6,961,953
Due from affiliates	501,858	2,127,771
Federal and state income tax receivable	—	598,970
Other current assets	921,435	861,950
Total current assets	7,139,004	15,358,085
Property and equipment, net	1,684,707	1,791,682
Goodwill, net	4,463,747	—
Other assets, net	1,346,896	1,575,083
Total assets	<u>\$14,634,354</u>	<u>18,724,850</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and other accrued expenses	\$ 2,643,761	1,546,762
Accrued network service costs	4,217,206	4,319,198
Sales and excise taxes payable	1,433,483	736,012
Unearned revenue	954,101	—
Due to affiliates	324,020	2,719,417
Other current liabilities	589,392	466,039
Total current liabilities	10,161,963	9,787,428
Deferred income taxes	—	498,712
Long term borrowings	1,112,890	—
Other liabilities	5,381	50,782
Common stock subject to put option (note 4)	168,867	578,880
Total liabilities	<u>11,449,101</u>	<u>10,915,802</u>
Stockholders' equity:		
Preferred stock, authorized 750,000 shares, \$0.01 par value.	—	—
Series A convertible preferred stock, authorized 250,000 shares, \$0.01 par value, cumulative as to 8% dividends, 147,700 and 207,700 shares issued and outstanding at December 31, 1998 and 1997 respectively. (Liquidation preference of \$704,032 December 31, 1998 including dividends in arrears.)	1,477	2,077
Common stock, Authorized 20,000,000 shares, \$0.01 par value; issued 10,409,473 and 11,437,056 shares at December 31, 1998 and 1997 respectively, including 112,578 and 385,920 shares subject to put options on December 31, 1998 and 1997 respectively.	102,969	110,511
Additional paid in capital	19,630,404	17,138,739
Accumulated deficit	(16,549,597)	(9,422,279)
Treasury stock, none at December 31, 1998 and 1,999,997 common shares at December 31, 1997.	—	(20,000)
Total stockholders' equity	<u>3,185,253</u>	<u>7,809,048</u>
Commitments and contingencies		
Total liabilities and stockholders' equity	<u>\$14,634,354</u>	<u>18,724,850</u>

See accompanying notes to consolidated financial statements.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
Years ended December 31, 1998, 1997 and 1996

	1998	1997	1996
Revenues (note 6)	\$44,013,498	51,389,080	71,558,295
Cost of revenues (note 6)	31,849,354	36,227,507	47,674,396
Gross margin	12,164,144	15,161,573	23,883,899
Operating expenses:			
Selling, general and administrative (note 6)	18,480,576	16,141,132	18,798,925
Acquisition related write off (note 2)	—	9,098,545	—
Depreciation and amortization	1,107,321	679,856	993,940
	19,587,897	25,919,533	19,792,865
Operating income (loss)	(7,423,753)	(10,757,960)	4,091,034
Interest expense (note 6)	(86,251)	(11,692)	(230,922)
Other income, net	181,107	301,580	393,498
Income (loss) before income tax expense	(7,328,897)	(10,468,072)	4,253,610
Income tax expense (benefit)	(201,579)	(276,352)	1,686,876
Net income (loss)	\$(7,127,318)	(10,191,720)	2,566,734
Net loss per common share—basic and diluted (note 8)	\$ (0.74)	(1.23)	
Weighted average number of common shares	9,633,474	8,267,296	

See accompanying notes to consolidated financial statements.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES

Consolidated Statements of Stockholders' Equity

Years ended December 31, 1998, 1997 and 1996

	Preferred Stock		Common Stock		Additional Paid in Capital	Retained Earnings (accumulated deficit)	Treasury Stock		Total
	Shares	Amount	Shares	Amount			Shares	Amount	
Balances at December 31, 1995	—	—	6,872,883	5,336,815	—	(1,797,293)	—	—	3,539,522
Purchase of common stock	—	—	—	—	—	—	(171,548)	(439,584)	(439,584)
Issuance of common stock	—	—	1,463,771	2,195,211	—	—	—	—	2,195,211
Net income	—	—	—	—	—	2,566,734	—	—	2,566,734
Balances at December 31, 1996	—	—	8,336,654	7,532,026	—	769,441	(171,548)	(439,584)	7,861,883
Acquisition of Best (note 2)	—	—	934,987	3,361,208	—	—	(1,999,997)	(3,317,940)	43,268
Share for share exchange between AvTel and Matrix (note 2):									
Reverse acquisition of AvTel	207,700	2,077	1,839,563	18,396	9,129,040	—	—	—	9,149,513
Reflect new capitalization of Company	—	—	(171,548)	(10,802,234)	7,064,710	—	171,548	3,737,524	—
Issuance of common stock for exercise of options	—	—	15,000	150	52,350	—	—	—	52,500
Expired put options (note 4)	—	—	96,480	965	143,755	—	—	—	144,720
Stock compensation earned (note 7)	—	—	—	—	748,884	—	—	—	748,884
Net loss	—	—	—	—	—	(10,191,720)	—	—	(10,191,720)
Balances at December 31, 1997	207,700	\$2,077	11,051,136	\$ 110,511	17,138,739	(9,423,279)	(1,999,997)	\$ (20,000)	7,809,048
Conversion of preferred stock (note 4)	(60,000)	(600)	60,000	600	—	—	—	—	—
Issuance of common stock for exercise of options and restricted common stock	—	—	473,326	4,733	512,879	—	—	—	517,612
Issuance of common stock for acquisitions (note 2)	—	—	680,000	6,800	1,526,950	—	—	—	1,533,750
Expired put options (note 4)	—	—	48,187	482	36,770	—	—	—	37,252
Exercised put options (note 6)	—	—	185,847	1,859	372,918	—	(201,604)	(2,016)	372,761
Purchase of officer notes receivable (note 6)	—	—	—	—	(435,000)	—	—	—	(435,000)
Stock compensation earned (note 7)	—	—	—	—	477,148	—	—	—	477,148
Retirement of treasury stock	—	—	(2,201,601)	(22,016)	—	—	2,201,601	22,016	—
Net loss	—	—	—	—	—	(7,127,318)	—	—	(7,127,318)
Balances at December 31, 1998	147,700	\$1,477	10,296,895	\$ 102,969	19,630,404	(16,549,597)	—	\$ —	3,185,253

See accompanying notes to consolidated financial statements.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years ended December 31, 1998, 1997 and 1996

	1998	1997	1996
Cash flows from operating activities:			
Net income (loss)	\$(7,127,318)	\$(10,191,720)	2,566,734
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	1,107,321	679,856	993,940
Amortization of advanced commissions	220,928	1,355,492	618,791
Acquisition related write off	—	9,098,545	—
Gain on disposition of assets	(83,139)	—	—
Provision for bad debts	2,727,803	1,829,770	1,461,471
Deferred income taxes	(498,712)	(80,377)	(321,678)
Stock compensation earned	477,148	748,884	—
Equity in income of DNS	—	—	(122,327)
Changes in certain operating assets and liabilities:			
Accounts receivable	374,477	1,969,332	(1,971,970)
Due from affiliates	(106,071)	(915,357)	345,336
Federal and state income tax receivable	583,906	(598,970)	—
Other current assets	(224,820)	1,787,672	(393,781)
Accounts payable and accrued liabilities	(1,034,923)	(2,876,789)	(1,397,160)
Due to affiliates	(2,395,397)	(1,138,568)	(742,663)
Net cash provided by (used in) operating activities	(5,978,797)	1,667,770	1,036,693
Cash flows from investing activities:			
Cash received (paid) in acquisitions (note 2)	(474,082)	477,643	—
Loans to affiliate	—	(2,000,000)	—
Payments received on loans to affiliates	1,798,889	201,111	—
Purchase of property and equipment	(473,089)	(212,421)	(701,718)
Repayments from DNS, net	—	—	1,577,432
Proceeds from sale of property and equipment	94,370	2,749	(14,482)
Net cash provided by (used in) investing activities	946,088	(1,530,918)	861,232
Cash flows from financing activities:			
Principal payments on capital leases	(59,055)	(4,306)	—
Issuance of common stock for exercise of options	517,612	52,500	—
Borrowings on line of credit	9,753,467	—	—
Amounts paid on line of credit	(8,640,577)	—	—
Purchase of officer notes receivable	(435,000)	—	—
Purchase of common stock for treasury	—	—	(439,583)
Net cash provided by (used in) financing activities	1,136,447	48,194	(439,583)
Net increase (decrease) in cash and cash equivalents	(3,896,262)	185,046	1,458,342
Cash and cash equivalents at beginning of year	4,807,441	4,622,395	3,164,053
Cash and cash equivalents at end of year	\$ 911,179	\$ 4,807,441	4,622,395
Cash paid (received) during the year for:			
Interest	\$ 86,121	11,594	212,404
Income taxes, net of refunds	\$ (487,007)	925,161	1,482,103
Noncash financing activities:			
Common stock issued for advanced commissions	\$ —	—	2,195,211
Common stock issued for receivable from major shareholder	\$ —	—	723,600
Common stock issued for Best acquisition	\$ —	3,361,208	—
Treasury stock acquired with Best acquisition	\$ —	(3,317,940)	—
Common and preferred stock issued in AvTel reverse acquisition	\$ —	9,149,513	—
Common stock issued for DMI acquisition	\$ 30,000	—	—
Common stock issued for RLI acquisition	\$ 650,000	—	—

See accompanying notes to consolidated financial statements.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1996, 1997, and 1996

(1) Summary of Significant Accounting Policies

(a) Business and Background

On December 1, 1997, AVTel Communications, Inc. ("AVTel") and Matrix Telecom, Inc. ("Matrix") completed a share for share exchange pursuant to a stock exchange agreement dated April 29, 1997 as subsequently amended ("Share Exchange"). For accounting purposes, the Share Exchange was treated as a reverse acquisition of AVTel by Matrix. AVTel was the legal acquirer and accordingly, the Share Exchange was effected by the issuance by AVTel of 9,582,493 shares of common stock in exchange for all of the common stock then outstanding of Matrix. In addition, holders of outstanding Matrix stock options received 22,338 non-qualified stock options of AVTel. The purchase method of accounting was used, with Matrix being treated as the acquirer for accounting purposes. The results of operations reported in the accompanying consolidated financial statements reflect the operations of Matrix prior to December 1, 1997 and the combined operations of AVTel and Matrix subsequent to December 1, 1997. References to the "Company" refer to operations of Matrix prior to the Share Exchange and the combined operations of Matrix and AVTel subsequent to the Share Exchange. As a result of the Share Exchange, Matrix became a wholly owned subsidiary of AVTel. (See note 2).

The Share Exchange provided that each Matrix shareholder would receive 2.4819 AVTel common shares for each common share of Matrix then issued including treasury shares held by Matrix. For periods prior to the December 1, 1997 Share Exchange, all share amounts have been restated to reflect the Share Exchange as a 2.4819 for one stock split. In addition, on March 10, 1997 Matrix declared an 18 for one stock split. All share amounts have also been restated to reflect this stock split.

AVTel was formed to be a provider of broadband network services integrating voice, data and Internet solutions for individuals and corporate customers. The Company sells and markets a broad range of telecommunications and advanced network services through independent value added resellers, third party marketing organizations and internal direct sales professionals. The Company targets mid-size corporations, small-office home-office professionals and select residential market segments through two primary business units, its Business Markets Group ("BMG") and Channel Markets Group ("CMG").

BMG targets mid-size corporate customers for their broadband data, voice and Internet networking needs. Following this sales strategy, the Company's objective is to become the underlying telecommunications carrier for the transport of data, voice and Internet traffic. Through a value-added sales process, the Company designs, provisions and manages its customers' network. The Company will provide a host of additional value-added services assisting its customers to create enhanced intranet and extranet applications. Additionally, BMG markets to its customer base a variety of traditional communications products and services such as long distance telephone service, executive calling cards and video/audio conferencing.

CMG targets and markets to distribution companies, agents, resellers and affinity groups that maintain access to large groups of individuals and small businesses through affinity relationships and niche marketing strategies. CMG provides Internet access, long distance telephone and other services to customers in 49 states. The Company is fully certified or registered in all states where required and operates under Section 214 authority from the Federal Communications Commission ("FCC"). The Company, through a wholly owned subsidiary, has a national-deployed Carrier Identification Code ("CIC"). The Company maintains its own convergent billing platform, rating system and monitoring center.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(1) Summary of Significant Accounting Policies (Continued)

(b) Liquidity

The Company's consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. As shown in the consolidated financial statements during the years ended December 31, 1998 and 1997, the Company reported net losses of \$7,127,318 and \$10,191,720, respectively. In addition, as of December 31, 1998, the Company had a working capital deficit of \$3,022,959, and for the year ended December 31, 1998, net cash used in operations totaled \$5,978,797.

As a result, as of December 31, 1998, unless the Company effects substantial changes in its operating methods, the Company does not have sufficient resources to meet its anticipated operating requirements during 1999 without obtaining additional financing. The Company is actively pursuing an equity line of credit through discussion with potential investors. If the Company is unable to obtain financing in a timely manner and on acceptable terms, management is developing and intends to implement a plan that would allow the Company to continue to operate through 1999. This plan would include significantly reducing the Company's workforce, eliminating advertising expenditures, reducing professional services and reducing or eliminating other discretionary expenditures.

(c) Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

(d) Cash and Cash Equivalents

For purposes of the statement of cash flows, the Company considers all demand deposits, time deposits, and other highly liquid investments with a remaining maturity at date of purchase of less than ninety days to be cash equivalents.

(e) Commissions

Commissions to sales agents are paid and expensed based on a percentage of billings as incurred.

Commissions paid in advance of \$221,000 as of December 31, 1997, included in other current assets, were expensed over a period of eighteen months based on estimated billings of the customers for which the commissions were paid. The above advances were fully expensed during 1998 and no additional advance commission payments were made.

(f) Revenue Recognition

Long distance, frame relay, Internet, systems integration and repair service revenues are recognized as service is provided. Amounts paid in advance are recorded as unearned revenue and recognized as services are provided.

(g) Property and Equipment

Property and equipment are recorded at cost. Maintenance and repairs are charged against income as incurred, while renewals and major replacements are capitalized. The cost and related accumulated depreciation of assets sold or retired are removed from the accounts, and any resulting gain or loss is

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(1) Summary of Significant Accounting Policies (Continued)

reflected in operations. The Company provides depreciation on fixed assets using the straight-line method over the estimated useful lives of the respective assets.

(h) Goodwill

Goodwill of \$4.5 million, which is net of amortization of \$19,000 as of December 31, 1998, represents the excess of purchase price over fair value of net assets acquired in the DMI and RLI acquisitions and is amortized on a straight-line basis over fifteen years. The Company assesses the recoverability of this intangible asset by determining whether the amortization of the goodwill balance over its remaining life can be recovered through undiscounted future cash flows of the acquired operation. The amount of goodwill impairment, if any, is measured based on expected undiscounted future operating cash flows expected to be generated by the acquired business. The assessment of the recoverability of goodwill will be impacted if estimated future operating cash flows are not achieved.

(i) Income Taxes

The Company utilizes the asset and liability method for accounting for income taxes. Under this method, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

(j) Use of Estimates

Management of the Company has made a number of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period to prepare these consolidated financial statements in conformity with generally accepted accounting principles. Actual results could differ from those estimates.

(k) Concentrations of Credit Risk

The Company's subscribers are primarily small business owners and residential subscribers and are not concentrated in any specific geographic region of the United States. The Company has agreements with Local Exchange Companies, which provide billing and collection services to the majority of the Company's subscribers. A significant portion of the Company's accounts receivable is due from these companies.

(l) Accounts Receivable

Accounts receivable are net of allowances for doubtful accounts and other provisions of \$935,000 and \$982,000 as of December 31, 1998 and 1997, respectively. The Company establishes an allowance for doubtful accounts based upon factors surrounding the credit risk of subscribers, historical trends and other information.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 31, 1998, 1997, and 1996

(l) Summary of Significant Accounting Policies (Continued)

(m) Financial Instruments

The Company's financial instruments include cash, receivables, payables, and accrued expenses. The carrying amount of such financial instruments approximates fair value because of the short maturity of these instruments.

(n) Acquired Customer Base

Acquired customer base of \$1,240,000, which is net of accumulated amortization of \$343,000 at December 31, 1998, included in other assets, is being amortized on a straight-line basis over five years. The Company assesses the recoverability of this intangible asset by determining whether the acquired customer base balance can be recovered through undiscounted future operating cash flows of the acquired operations. The amount of impairment, if any, is measured based on projected discounted cash flows. The assessment of the recoverability of the acquired customer base will be impacted if estimated future operating cash flows are not achieved.

(o) Impairment of Long-Lived Assets

In January, 1996, the Company adopted Statement of Financial Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of" ("SFAS No. 121"), SFAS No. 121 requires that long-lived assets and certain intangibles be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the net asset exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less costs to sell.

(p) Comprehensive Income

In 1998, the Company adopted Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" ("SFAS No. 130"). SFAS No. 130 establishes standards for reporting and presentation of comprehensive income and its components in a full set of financial statements. Comprehensive income includes net income and other comprehensive income, which is generally composed of changes in the fair value of available-for-sale marketable securities, foreign currency translation adjustments and adjustments to recognize additional minimum pension liabilities. The statement requires additional disclosures in the consolidated financial statements; it does not affect the Company's financial position or results of operations. Comprehensive income (loss) for the years ended December 31, 1998, 1997 and 1996 is equal to net income (loss) reported for such periods.

(q) Segment Reporting

In 1998, the Company adopted the provisions of Statement of Financial Accounting Standards No. 131, "Disclosures About Segments of an Enterprise and Related Information" (SFAS No. 131"), SFAS No. 131 establishes standards for the way that public business enterprises report information about operating segments in annual financial statements and requires that those enterprises report selected information about operating segments in interim financial reports issued to shareholders. It also establishes standards for related disclosures about products and services, geographic areas and major customers. (See Note 11).

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 31, 1998, 1997, and 1996

(1) Summary of Significant Accounting Policies (Continued)

(c) Reclassifications

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

(2) Acquisitions

Matrix Telecom, Inc.—On December 1, 1997, AVTel and Matrix completed the Share Exchange. For accounting purposes the Share Exchange was treated as a reverse acquisition of AVTel by Matrix. AVTel was the legal acquirer and, accordingly, the Share Exchange was effected by the issuance of AVTel common stock in exchange for all of the common stock then outstanding of Matrix. In addition, holders of outstanding Matrix stock options received non-qualified stock options of the Company. Immediately after the Share Exchange the former shareholders of Matrix held approximately 84% of the then outstanding common stock of the Company.

The consummation of the Share Exchange was subject to the satisfaction of several conditions by AVTel. These included the reincorporation of AVTel (then a Utah corporation, "AVTel Utah") in Delaware by way of a merger (the "Reincorporation Merger") with and into AVTel Communications, Inc., a Delaware corporation, a wholly-owned subsidiary formed for the sole purpose of this merger. As part of the merger, AVTel (the surviving Delaware corporation) issued to its stockholders one share of new Delaware Common Stock for each four shares of AVTel-Utah's Common Stock outstanding immediately prior to the Reincorporation Merger. AVTel's Series A Convertible Preferred Stock and its outstanding options were similarly adjusted. Accordingly, the Reincorporation Merger essentially effected a one for four reverse stock split of AVTel's shares.

The reverse acquisition of AVTel by Matrix was accounted for using the purchase method of accounting. In order to value the consideration given in the Share Exchange the market price of AVTel's common stock for a period immediately preceding the announcement of the Share Exchange was used. As of the date of acquisition, the Company determined the fair value of the net tangible and intangible assets acquired and liabilities assumed. Concurrently, the Company determined that the carrying amount of recorded goodwill was not recoverable. Accordingly, the Company recorded a charge to income of \$9,096,545 immediately subsequent to the reverse acquisition.

In connection with the completion of the Share Exchange, the Company entered into a Registration Rights and Lockup Agreement dated December 1, 1997 (the "Registration Rights and Lockup Agreement"). The Registration Rights and Lockup Agreement requires that the Company use its best efforts to file a shelf registration statement providing for the sale by certain stockholders of all securities issued to them in connection with the Exchange Agreement, subject to a two-year holding restriction imposed on such stockholders. Under the Registration Rights and Lockup Agreement, the Company is obliged to use its reasonable efforts to keep the shelf registration statement effective on a continuous basis for a period described in the Registration Rights and Lockup Agreement. Such stockholders may also require the Company to undertake up to two additional demand registrations of their securities if the shelf registration is not in place. As of April 14, 1999, this registration obligation related to 6,457,123 shares held by 14 stockholders.

Best Connections, Inc. ("Best")—Effective July 1, 1997, shareholders of Best, an affiliate of Matrix through substantially common ownership, contributed their ownership of Best to Matrix in exchange for

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 31, 1998, 1997, and 1996

(2) Acquisitions (Continued)

934,987 shares of Matrix common stock. Best's primary assets were 1,999,997 shares of Matrix common stock and cash of \$211,000. The assets and liabilities of Best were recorded at their historical cost which approximated the fair value of such assets as of July 1, 1997. As a result of the combination, Matrix assumed the obligation to grant up to 1,999,997 stock options to agents of Best and certain employees of affiliated companies. Such option grants relate to services, including sales promotion activities, to be performed by the recipients on behalf of the Company. Accordingly, the fair value of such options is being charged to expense by the Company as the related services are provided.

Digital Media, Inc. ("DMI")— Effective September 25, 1998, the Company acquired all of the capital stock of DMI, a California based developer of multimedia software. The Company exchanged 30,000 shares of its common stock valued at \$71,250 for all of the outstanding common stock of DMI. The transaction was accounted for under the purchase method of accounting. The assets and liabilities of DMI were recorded at their historical cost which approximated their fair value at September 25, 1998. The Company recorded goodwill of approximately \$117,000, which represents the excess of the purchase price over the fair value of the net assets received. The goodwill is being amortized on a straight-line basis over fifteen years.

Remote Lojix/PCSI, Inc. ("RLI")— Effective November 1, 1998, the Company acquired all of the capital stock of RLI, a New York based provider of information technology services to corporate customers. The Company exchanged 650,000 shares of its common stock valued at \$1,462,500 and the outstanding balance of a \$500,000 loan from the Company for all of the outstanding common stock of RLI. The transaction was accounted for under the purchase method of accounting. The assets and liabilities of RLI were recorded at their historical cost which approximated the fair value at November 1, 1998. The Company recorded goodwill of approximately \$4.4 million, which represents the excess of the purchase price over the fair value of the assets received. The goodwill is being amortized on a straight-line basis over fifteen years.

Unaudited pro forma results of operations of the Company as if the share exchange of Matrix and the acquisitions of Best, DMI and RLI had occurred as of the beginning of the periods presented is as follows:

	Year Ended December 31	
	1998	1997
Revenue	\$ 49,711,440	\$ 58,967,268
Loss from operations	(8,909,490)	(12,749,469)
Net loss	(9,124,180)	(12,378,014)
Proforma net loss per share	\$ (0.89)	\$ (1.02)

The pro forma financial information has been prepared for comparative purposes only and does not purport to indicate the results of operations that would have occurred had the acquisition been made at the beginning of the period indicated, or which may occur in the future.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(2) Acquisitions (Continued)

As of the date of acquisitions, the fair market value of the assets acquired and liabilities assumed included the following:

	1998		
	DMI	RLI	Total
Current assets other than cash	\$ 50,105	1,034,803	1,084,908
Property and equipment	44,313	132,169	176,482
Goodwill	117,169	4,375,191	4,492,360
Current liabilities	(166,255)	(3,579,663)	(3,745,918)
Common stock issued	(71,250)	(1,462,500)	(1,533,750)
Cash acquired (paid)	\$ 25,918	(500,000)	(474,082)

	1997		
	Matrix	Best	Total
Current assets other than cash	\$ 258,041	—	258,041
Property and equipment	577,836	15,137	592,973
Customer base	1,583,000	—	1,583,000
Goodwill	9,098,545	—	9,098,545
Current liabilities	(1,945,526)	(183,041)	(2,128,567)
Long-term liabilities	(688,854)	—	(688,854)
Common and preferred stock issued	(9,149,513)	(3,361,208)	(12,510,721)
Treasury stock acquired	—	3,317,940	3,317,940
Cash acquired	\$ 266,471	211,172	477,643

(3) Property and Equipment

Property and equipment consisted of the following:

	Estimated Useful Life	December 31	
		1998	1997
Communications system	2-5 years	\$ 1,318,326	\$ 1,318,326
Office furniture and equipment	1-7 years	3,420,773	2,945,795
Leasehold improvements	lease term	521,319	416,220
Total property and equipment		5,260,418	4,680,341
Accumulated depreciation and amortization		(3,575,711)	(2,888,659)
Property and equipment, net		\$ 1,684,707	\$ 1,791,682

Depreciation expense was \$737,000, \$632,000 and \$877,000 for 1998, 1997 and 1996, respectively.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 31, 1998, 1997, and 1996

(4) Stockholders' Equity

The Series A convertible preferred shareholders are entitled to receive cumulative annual dividends at a rate of 8% and are entitled to a preference in liquidation in the amount of \$4 per share plus unpaid dividends. There were \$137,000 cumulative Series A convertible preferred stock dividends in arrears at December 31, 1998. The Series A preferred stock is convertible, on a one-for-one basis, into shares of Company common stock. During 1998, a total of 60,000 shares of the Company's Series A convertible preferred stock was converted to 60,000 shares of the Company's common stock.

In December 1998, the Company retired all of its outstanding treasury stock.

In December 1996, the Company issued 1,463,771 shares of common stock for future commissions due to affiliates as of October 31, 1996. A value of \$1.50 per share was used in determining the number of shares to issue in settlement of the \$2,195,211 obligation. Of this amount, \$221,000, \$1,355,000 and \$619,000 was expensed as commission expense in 1998, 1997 and 1996, respectively.

During 1996, the Company sold to certain employees 482,400 shares of common stock at \$1.50 per share. As of December 31, 1996, the Company had recorded a \$723,600 receivable for such shares, which was subsequently collected. Proceeds used to repay the \$723,600 receivable were loaned to the employees by a major shareholder of the Company. As of December 31, 1998 and 1997, the shares subject to this agreement could be put to the Company at the option of the employee at approximately \$1.50 per share (\$168,867 and \$578,880), respectively. Such amounts have been included in other liabilities. Under certain circumstances (e.g. employee termination) the Company has a call at the same amount. The call and put rights vest over a period of five years. As of December 31, 1998, these rights were forty percent vested. Activity in common stock outstanding related to shares subject to put follows:

	Shares	Amount
Sale of common shares subject to put	482,400	\$ 723,600
Increase in share value subject to put charged to expense	<u>—</u>	<u>172,400</u>
Balance, December 31, 1996	482,400	896,000
Decrease in share value subject to put recorded as a reduction to expense	<u>—</u>	<u>(172,400)</u>
Vested shares no longer subject to put	<u>(96,480)</u>	<u>(144,720)</u>
Balance, December 31, 1997	385,920	578,880
Vested shares no longer subject to put	<u>(48,187)</u>	<u>(37,253)</u>
Called shares subject to put	<u>(225,155)</u>	<u>(372,760)</u>
Balance, December 31, 1998	<u>112,578</u>	<u>\$ 168,867</u>

During May 1996, the Company purchased 171,548 shares of its common stock as treasury stock for \$439,584. As further discussed in note 8 in connection with the Best and Matrix combination effective July 1, 1997, Matrix acquired an additional 1,999,997 shares of its common stock as treasury stock. As a part of the recapitalization done in connection with the AvTel reverse acquisition, Matrix retired the 171,548 shares of its common stock discussed above and the Company recorded the remaining treasury stock at par value.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(5) Federal and State Income Taxes

The provision for income taxes consisted of the following:

	1998	1997	1996
Current tax expense (benefit):			
Federal	\$ —	\$(234,899)	\$1,751,047
State and local	7,531	(41,453)	257,507
	<u>7,531</u>	<u>(276,352)</u>	<u>2,008,554</u>
Deferred tax expense (benefit):			
Federal	(209,110)	—	(254,350)
State and local	—	—	(67,328)
	<u>(209,110)</u>	<u>—</u>	<u>(321,678)</u>
	<u><u>\$(201,579)</u></u>	<u><u>\$(276,352)</u></u>	<u><u>\$1,686,876</u></u>

Income tax expense differs from the amounts computed by applying the U.S. federal income tax rate of 34 percent to pretax income as a result of the following:

	1998	1997	1996
Computed "expected" tax expense (benefit) .	\$(2,491,825)	\$(3,559,144)	\$1,404,637
State and local taxes, net of federal income tax effect	(135,961)	(27,359)	125,518
Other nondeductible items	22,539	3,093,522	—
Losses not providing tax benefit	2,594,289	330,190	—
Other	(190,621)	(113,561)	156,721
	<u>\$ (201,579)</u>	<u>\$ (276,352)</u>	<u>\$1,686,876</u>

Deferred income taxes as of December 31, 1998 and 1997 reflect the impact of temporary differences between financial statement carrying amounts and tax bases of assets and liabilities. The tax effects of

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 31, 1998, 1997, and 1996

(5) Federal and State Income Taxes (Continued)

temporary differences that give rise to significant portions of the net deferred tax assets at December 31, 1998 and 1997 are presented below:

	December 31	
	1998	1997
Deferred tax assets		
Net operating loss carryovers	\$ 3,494,634	\$ 814,425
Compensation related items	480,137	299,554
Contingent liabilities and other	268,340	204,978
Gross deferred tax asset	4,243,111	1,318,957
Less valuation allowance	(3,778,958)	(1,184,669)
Net deferred tax asset	464,153	134,288
Deferred tax liabilities:		
Customer base intangible	(464,153)	(633,000)
Net deferred tax liability	\$ —	\$ (498,712)

The valuation allowance for deferred tax assets increased \$2,594,289 and \$1,184,669 during 1998 and 1997, respectively.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and prior taxes paid in making this assessment. Based upon its evaluation of these factors, management believes that it is more likely than not that the Company will realize the benefits of these deductible differences, net of the valuation allowance, at December 31, 1998. At December 31, 1998, the Company has net operating loss carryforwards for federal tax purposes of approximately \$9,153,822 which are available on a limited basis to offset future federal taxable income, if any, through 2018. When realized, such benefit will first be utilized to reduce intangible assets recorded in the reverse acquisition of AvTel by Matrix.

(6) Related Party Transactions

The Company has had transactions in the normal course of business with various companies which are affiliated with shareholders of the Company. Pacific Gateway Exchange, Inc. ("PGE") provides the Company with significant domestic and international transmission services. As of January 1, 1998, PGE was no longer affiliated with the Company. During 1998, a director and several significant holders of the Company's common stock divested themselves of a substantial portion of their holdings of PGE common stock; they have advised the Company that they no longer could be deemed to be in control of PGE. A significant number of the Company's employees were leased from United Group Service Center, an affiliate, which provides such services to a number of affiliated companies. This lease agreement was terminated on December 31, 1998, at which time these individuals became employees of the Company. The Company provides long distance and data network service to a number of affiliated companies.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(6) Related Party Transactions (Continued)

Balances with affiliates related to operating activities are settled monthly. In addition, the Company has made both interest bearing and non-interest bearing advances to affiliated companies.

Due from affiliates consists of the following:

	December 31	
	1998	1997
Core Marketing—note receivable due September 1, 1998 . . .	\$ —	\$1,798,889
UICI Administrators (long distance services)	308,346	94,417
Interactive Media Works (IMW) (long distance services) . . .	6,214	25,263
Core Marketing (long distance services)	82,695	111,280
AMLI Management Co. (long distance services)	10,695	—
Other receivables from various affiliates	93,908	97,922
	<u>\$501,858</u>	<u>\$2,127,771</u>

Due to affiliates consists of the following:

	December 31	
	1998	1997
PGE (not considered an affiliate in 1998)	\$ —	2,335,787
Group Association (UGA) and Core Marketing (commissions)	5,339	134,618
Other payables to various affiliates	318,681	249,012
	<u>\$324,020</u>	<u>2,719,417</u>

ATTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(6) Related Party Transactions (Continued)

Significant services and transactions incurred in the normal course of operations with affiliated companies are summarized as follows:

	1998	1997	1996
Revenues include the following:			
U.S. Teico-billing and collection services, customer service and accounting services	\$ —	\$ 200,370	\$ —
Long distance revenues from affiliates: UGA, UICI, IM/W, Core Marketing, and AMIL	<u>4,592,040</u>	<u>3,351,375</u>	<u>5,445,903</u>
	<u>\$4,592,040</u>	<u>\$3,551,745</u>	<u>\$ 5,445,903</u>
Cost of revenues includes the following:			
Network transmission services—PGE (not considered an affiliate in 1998)	\$ —	<u>15,917,688</u>	<u>20,527,236</u>
Selling, general and administrative expenses include the following:			
Expenses paid on behalf of PGE (not considered an affiliate in 1998) for access services, for which the Company was reimbursed	\$ —	3,534,154	5,040,051
Expenses incurred for leasing employees from United Group Service Center	5,581,428	4,395,820	4,542,007
Sales commissions to affiliates:			
Core Marketing, UICI, UGA, Best Connections and AMIL	140,187	990,533	5,335,233
Overhead expenses reimbursed to/from UGA Divisions	241,810	110,761	77,231
Core Marketing—casual mailings and telemarketing	<u>21,425</u>	<u>603,742</u>	<u>—</u>
	<u>\$5,984,850</u>	<u>\$9,635,010</u>	<u>\$14,994,522</u>
Interest expense includes the following:			
Interest paid to shareholder	\$ —	\$ —	\$ 173,380

During 1997, the Company loaned \$2,000,000 to an affiliated company, Core Marketing, LLC. Of such amount, \$201,000 was repaid in 1997 and the remainder was repaid in 1998.

In July 1998, the Company purchased notes receivable from one of the Company's significant shareholders at a discount. The notes receivable evidenced loans made by the significant shareholder in 1996 to Matrix employees to finance their purchases of Matrix common stock (which was subsequently converted to shares of the Company's common stock). Each of the employees who delivered a note receivable also entered into a Buyback Agreement dated October 6, 1996 (the "Buyback Agreement"), pursuant to which the Company has the option (but no obligation) to repurchase a portion of such employee's stock upon the termination of his or her employment. The original notes, plus accrued interest, at the date of purchase by the Company was \$573,000. The Company purchased these notes for \$435,000.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 31, 1998, 1997, and 1996

(6) Related Party Transactions

In connection with the purchase of the notes receivable above, the Company repurchased 240,912 shares of its common stock subject to the Buyback Agreement from terminated employees. The Company exercised its right to repurchase 225,154 of such shares at a price range of \$1.51 to \$1.70 per share, and the former employees used the \$373,081 in proceeds to reduce the amount of their notes. The Company repurchased an additional 15,758 shares in satisfaction of the remaining balance of \$116,085 on the former employees' notes.

(7) Stock Compensation

AVTel options—Prior to the Share Exchange AVTel adopted a 1997 Incentive Stock Option Plan (the "AVTel 1997 Plan") for option grants to officers and key employees. The AVTel 1997 Plan authorizes grants of options to purchase up to 250,000 shares of authorized but unissued common stock and 125,000 shares of restricted common stock. Stock options are to be granted with an exercise price greater than or equal to the stock's fair market value at the date of grant. Options generally vest 25% after one year and 25% each year thereafter until fully vested. Such options typically expire after ten years. In addition, AVTel had other options which had been granted prior to the adoption of the AVTel 1997 Plan. After the Share Exchange all outstanding options became obligations of the Company.

On January 1, 1998, the Company granted options to purchase 75,000 shares of the Company's common stock at an exercise price of \$1.50 per share. On March 1, 1998 the Company granted options to purchase 100,000 shares of the Company's common stock at an exercise price of \$1.50 per share. These options become exercisable based on qualified billings of long distance customers generated by the optionees from the respective dates of grant through December 31, 2000. As of December 31, 1998, 27,316 options are exercisable.

On February 24, 1998, the Company's Board of Directors approved the grant of a total of 120,000 shares of restricted common stock to two board members pursuant to the Company's 1997 Stock Incentive Plan. The restricted stock provisions will lapse over four years or fully lapse in the event of death or permanent disability of the grantees. During 1998 one of the board members resigned from the board and his 60,000 shares were vested immediately. As of December 31, 1998, only those 60,000 shares of restricted common stock are vested.

During 1998, the Company adopted the 1998 Stock Incentive Plan (the "AVTel 1998 Plan"), which provides for the issuance of up to 1,500,000 shares of AVTel common stock pursuant to stock options and issuances of restricted stock, as well as for the grant of stock appreciation rights. Stock options are to be granted with an exercise price greater than or equal to the stock's fair market value at the date of grant. Options generally vest 25% after one year and 25% each year thereafter until fully vested. Such options typically expire after ten years. As of December 31, 1998, the Company granted 671,000 options under the AVTel 1998 Plan. Exercise prices range from \$2.375 to \$4.00 per share.

Matrix options—Prior to the Share Exchange, the Board of Directors of Matrix approved stock options for certain officers and employees. Stock option transactions of Matrix are included in the table below. At the time of the Share Exchange, Matrix had 22,338 options outstanding to purchase its common stock. In connection with the Share Exchange, the Company reissued these stock options and they vested immediately. These reissued options expire in December 2002.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(7) Stock Compensation (Continued)

The Company applies APB Opinion No. 25 in accounting for the AvTel 1997 Plan, 1998 Stock Incentive Plan and the Matrix options discussed above; and, accordingly, no compensation cost has been recognized for its stock options issued to employees in the financial statements. For stock options granted to non-employees, the Company accounts for such options in accordance with the requirements of SFAS No. 123. Had the Company determined compensation cost based on the fair value at the grant date for stock options issued to employees under SFAS No. 123, the Company's net loss in 1998 and 1997 would not have materially changed.

Best Connections, Inc. options—As discussed in Note 2, as a result of the Matrix combination with Best, Matrix assumed the obligation to issue stock options to Best's agents under Best's 1997 Option Plan. Effective as of the date of combination, July 1, 1997, 1,292,000 options to purchase Matrix common shares were granted to Best agents at \$1.50 per share, which will result in aggregate commission expense of approximately \$764,000 over the vesting period. The option price per share was \$1.50. The agents' options become exercisable no later than December 31, 1999 and may be exercised earlier based on qualified billings of long distance customers generated by the agents during six month measurement periods. After the Share Exchange such options became obligations of the Company. As of December 31, 1998, 641,532 options have been earned and 172,120 exercised under the Plan and the Company recorded expense totaling approximately \$132,000 and \$249,000 related to such options based on qualified billings for 1998 and 1997, respectively. Options generally expire two years from the date they become exercisable or sixty days subsequent to termination of employment.

The per share weighted average fair value of stock options granted on July 1, 1997 was \$.59 on the date of the grant using the Black-Scholes option—pricing model with the following weighted-average assumptions: expected volatility of 30%, risk-free interest rate of 6.0%, and an expected life of 3.5 years.

Best Connections, Inc. options and restricted stock agreements—As discussed in Note 2 as a result of the Matrix combination with Best, Matrix assumed the obligation to issue stock options, consisting of Matrix common shares owned by Best, to employees of affiliated companies. Effective July 15, 1997, the Company issued 247,500 options to purchase an equal number of shares of its common stock, at \$1.50 per share subject to the provisions of a Restricted Stock Agreement. The Restricted Stock Agreement includes a call provision by the Company that lapses 10 percent each six months beginning December 15, 1997 through June 15, 2002 or fully lapses in the event of death or permanent disability of the option holder. The call price is equal to the initial purchase price of \$1.50 plus the aggregate amount of net income or less the aggregate amount of net losses per share for each fiscal quarter beginning after December 15, 1997; provided that the call price could not be less than \$1.50 per share. During 1998 AvTel relinquished its right to call the shares which caused the options to vest immediately and to expire if not exercised before December 13, 1998. AvTel provided the holders the option of a "cashless" exercise by purchasing up to one half the shares issuable at \$3.00. The Company recognized expense over the life of the options in accordance with the provisions of SFAS No. 123 and recorded expense of \$500,000 in 1997 and a reduction of expense of \$170,000 in 1998. At December 31, 1998, 107,250 options had been exercised, 67,250 were used for the cashless exercise, 45,500 expired, and 27,500 were cancelled.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(7) Stock Compensation (Continued)

Stock option activity is as follows:

	Options	Weighted average Exercise Price
Outstanding at December 31, 1995	53,607	\$2.24
Canceled	(31,269)	2.24
Outstanding at December 31, 1996	22,338	2.24
AvTel options outstanding at time of Share Exchange ..	255,109	4.52
Granted	1,539,500	1.50
Exercised	(15,000)	3.50
Outstanding at December 31, 1997	1,801,947	1.78
Granted	1,024,500	3.31
Expired	(46,750)	1.54
Forfeited	(106,999)	1.91
Exercised	(353,327)	1.81
Outstanding at December 31, 1998	<u>2,319,371</u>	<u>2.45</u>
Exercisable at December 31, 1995	—	\$ —
Exercisable at December 31, 1996	3,574	2.24
Exercisable at December 31, 1997	349,972	2.21
Exercisable at December 31, 1998	524,849	2.16

Total expense recorded for stock based awards during 1998 and 1997 was \$477,148 and \$748,884, respectively.

The following table summarizes certain information about the Company's stock options at December 31, 1998.

Range of exercise prices	Options Outstanding			Options Exercisable	
	Number of options	Weighted average remaining contractual life	Weighted average exercise price	Number of options exercisable	Weighted average exercise price
\$ 1.50 - 2.25	1,427,218	2.5 years	\$ 1.57	462,334	\$ 1.54
2.38 - 3.30	303,749	8.5	2.92	26,736	2.93
4.00 - 6.00	555,112	9.9	4.02	2,487	4.00
6.75 - 8.00	17,093	8.9	7.47	17,093	7.47
12.00 - 14.00	16,199	8.1	12.77	16,199	12.77
	<u>2,319,371</u>	5.1	2.45	<u>524,849</u>	2.16

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 31, 1998, 1997, and 1996

(8) Earnings Per Common Share

The Company adopted the provisions of Statement of Financial Accounting Standards No. 128, *Earnings per Share* ("SFAS 128") in the fourth quarter of 1997, which required companies to present basic earnings per share and diluted earnings per share.

	1998	1997
Numerator:		
Net loss	\$(7,127,318)	(10,191,720)
Less preferred dividends	47,264	5,540
Loss applicable to common shareholders	<u>\$(7,174,582)</u>	<u>(10,197,260)</u>
Denominator:		
Weighted average number of common shares used in basic and diluted loss per common share	9,633,474	8,267,296
Basic and diluted loss per common share	<u>\$ (0.74)</u>	<u>(1.23)</u>

Per share amounts are not reflected for 1996 due to the recapitalization of the Company as a result of the reverse acquisition in 1997.

(9) Leasing Activities and Other Commitments

The Company leases office space and various equipment under operating leases expiring in various years through 2004. In the normal course of business, operating leases are generally renewed or replaced by other leases. Total rental expenses were \$546,000 in 1998, \$245,000 in 1997, and \$325,000 in 1996. Future minimum lease payments under non-cancelable operating leases (with initial or remaining lease terms in excess of one year) and future minimum capital lease payments as of December 31, 1998 are: 1999—\$731,000; 2000—\$688,000; 2001—\$426,000; 2002—\$307,000; and 2003—\$101,224.

Substantially all of the Company's switching and transmission facilities have been provided by two suppliers under negotiated contractual agreements. The Company purchases long distance services at certain per-minute rates, which vary depending on the time and type of call. At December 31, 1998, there are outstanding contractual agreements committing the Company to \$18,570,000 minimum usage through February 15, 2000.

(10) Revolving Line of Credit

In 1998, the Company entered into a Loan and Security Agreement with a bank, which provides for an asset-based revolving credit line with a floating interest rate of prime plus 2% (9.75% at December 31, 1998), payable monthly. The credit limit is the lesser of \$7,500,000 or a percentage of the amount of the Company's eligible receivables and other items. Borrowings are secured by substantially all of the assets of the Company. The agreement also calls for a minimum borrowing of \$1,500,000 with a two-year term. At December 31, 1998, there was \$1,112,890 outstanding under the agreement, and an additional \$1,655,000 was eligible for borrowing under the revolving credit line.

The Loan and Security Agreement contains restrictions on net worth, future acquisitions and other transactions.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(11) Segment Reporting

In June 1997, the Financial Accounting Standards Board issued Statement No. 131, *Disclosures About Segments of an Enterprise and Related Information*, which the Company adopted in 1998. The Company identifies such segments based on management responsibility. The Company's two primary business segments are Business Markets Group ("BMG") and Channel Markets Group ("CMG").

BMG targets mid-size corporate customers for their broadband data, voice and Internet networking needs. Through a value-added sales process, the Company designs, provisions and manages its customers' networks. The Company provides a host of additional value-added services assisting its customers to create enhanced intranet and extranet applications. Additionally, BMG markets to its customer base a variety of traditional communications products and services such as long distance telephone service, executive calling cards and wireless paging.

CMG targets and markets to distribution companies, agents, resellers and affinity groups ("Channel Partners") that maintain access to large groups of individuals and small businesses through affinity relationships and niche marketing strategies. Channel Partners include non-profit organizations and for-profit distribution groups. CMG provides Internet access, long distance telephone and other services to customers in 49 states.

During 1998, the Company measured and monitored the progress of BMG and CMG based on revenues from external customers and gross margin. The results for the year ended December 31, 1998 are as follows:

<u>Year Ended December 31, 1998</u>			
	<u>BMG</u>	<u>CMG</u>	<u>Total</u>
Revenue from external customers	\$6,338,114	37,675,384	44,013,498
Gross margin	1,846,895	10,317,249	12,164,144
Total assets	8,079,998	6,554,356	14,634,354
<u>Year Ended December 31, 1997</u>			
	<u>BMG</u>	<u>CMG</u>	<u>Total</u>
Revenue from external customers	\$5,791,993	45,597,087	51,389,080
Gross margin	1,715,205	13,446,368	15,161,573
Total assets	2,241,825	16,483,025	18,724,850
<u>Year Ended December 31, 1996</u>			
	<u>BMG</u>	<u>CMG</u>	<u>Total</u>
Revenue from external customers	\$6,368,460	65,189,835	71,558,295
Gross margin	2,135,461	21,748,438	23,883,899
Total assets	705,964	19,632,440	20,338,404

(12) Contingencies

The Company's common stock has been traded on The Nasdaq SmallCap Market since May 28, 1998. Trading in the Company's stock was halted by Nasdaq after the close of trading on November 12, 1998,

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

December 31, 1998, 1997, and 1996

(12) Contingencies (Continued)

through the close of trading on November 13, 1998, as a result of an unusual upsurge in its stock price and trading volume. This unusual event has triggered the initiation of class action litigation under the federal securities laws. The Company believes that these claims are without merit and intends to defend vigorously this litigation. However, it is not possible at this time for the Company to predict with certainty the outcome of this litigation. Even if the Company prevails in the litigation, the expenses of the defense could have a material adverse effect on the Company's operating results and financial condition.

The Company presently has other contingent liabilities relating to various lawsuits and other matters related to the conduct of its business. On the basis of information furnished by counsel and others, management believes these contingencies upon resolution will not materially affect the financial condition or results of operations of the Company.

(13) Subsequent Events

On April 13, 1999, the Company sold 1,500 shares of its newly-designated Series B Convertible Preferred Stock (the "Series B Stock") to AMRO International, S.A., an entity organized under the laws of Panama, Austinvest Anstalt Balzers, an entity organized under the laws of Liechtenstein, and Esquire Trade & Finance Inc., an entity organized under the laws of the British Virgin Islands (the "Series B Investors") for \$1,500,000. The Series B Stock has a liquidation preference of \$1,000 per share. The Series B Stock will be entitled to an annual dividend of \$30 per share, payable in cash or Common Stock, at the Company's option. The annual dividend will increase to \$60 per share if the Company ever ceases to be listed on The Nasdaq Stock Market or any national securities exchange. The Series B Stock is convertible into Common Stock at the option of the Series B Investors at any time. The number of shares of Common Stock to be received by a Series B Investor upon conversion will equal the liquidation preference of the amount converted, divided by the conversion price. The conversion price will be the lesser of (1) \$6.875, or (2) 89% of the low closing bid price for the Common Stock on The Nasdaq SmallCap Market at the time of conversion. The conversion price will not be less than \$3.00 for 180 days after the date of issuance of the Series B Stock. Thereafter the conversion price will not be less than \$2.00 as long as certain revenue and EBITDA requirements are met. As a result, the Company could issue up to 750,000 shares of Common Stock upon conversion if all of the Series B Stock were converted at the lowest possible conversion price (assuming such revenue and EBITDA requirements continue to be met). Unless the Company shall have obtained the approval of its voting stockholders in accordance with the rules of The Nasdaq Stock Market, the Company will not issue shares of Common Stock upon conversion of any shares of Series B Stock if such issuance of Common Stock, when added to the number of shares of Common Stock previously issued by the Company upon conversion of or as dividends on shares of the Series B Stock, would exceed 19.9% of the number of shares of Common Stock which were issued and outstanding on the original issuance date of the Series B Stock. The Company will pay converting Series B Investors in cash for any excess over such amount.

The Company also issued the Series B Investors warrants to purchase up to 20,000 shares of Common Stock at a price of \$8.60 per share. The warrants may be exercised beginning September 30, 1999, and terminate on March 31, 2002.

The Company and the Series B Investors entered into a Registration Rights Agreement that requires the Company to file, and obtain and maintain the effectiveness of, a Registration Statement with the Securities and Exchange Commission (the "Commission") in order to register the public resale of all

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
December 31, 1998, 1997, and 1996

(13) Subsequent Events (Continued)

shares of the Common Stock acquired by the Series B Investors (a) upon conversion of the Series B Stock, (b) in payment of dividends on the Series B Stock, and (c) upon exercise of the warrants. The Company will be subject to significant monetary penalties if it fails to obtain or maintain the effectiveness of such Registration Statement.

The Company paid Trinity Capital Advisors, Inc. \$60,000 as compensation for arranging the placement of the Series B Stock.

AVTEL COMMUNICATIONS, INC. AND SUBSIDIARIES
SCHEDULE II — VALUATION AND QUALIFYING ACCOUNTS
Years ended December 31, 1998, 1997, and 1996

<u>Description</u>	<u>Balance at beginning of period</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance at end of period</u>
Allowance for doubtful Accounts and other Provisions—years ended:				
December 31, 1998	<u>\$ 982,000</u>	<u>2,728,000(a)</u>	<u>2,775,000(b)</u>	<u>935,000</u>
December 31, 1997	<u>\$ 627,000</u>	<u>1,830,000(a)</u>	<u>1,475,000(b)</u>	<u>982,000</u>
December 31, 1996	<u>\$ 730,000</u>	<u>1,461,000(a)</u>	<u>1,564,000(b)</u>	<u>627,000</u>
Valuation allowance for deferred tax assets:				
December 31, 1998	<u>\$1,185,000</u>	<u>2,594,000(c)</u>	<u>—</u>	<u>3,779,000</u>
December 31, 1997	<u>\$ —</u>	<u>1,185,000(c)</u>	<u>—</u>	<u>1,185,000</u>
December 31, 1996	<u>\$ —</u>	<u>—</u>	<u>—</u>	<u>—</u>

(a) Charged to cost of revenues.

(b) Amounts written off.

(c) Recognized as a component of deferred tax assets.

EXHIBIT INDEX

<u>Exhibit Number</u>	<u>Title of Document</u>	<u>Page Number</u>
2.1	Acquisition Agreement, dated as of August 30, 1996, by and among Hi-Tiger International, Inc., a Utah corporation, AVTel Communications, Inc., a Utah corporation, and AVTel Holdings, Inc., a California corporation. (Incorporated by reference to Exhibit A to Registrant's Information Statement on Schedule 14C dated October 2, 1996).	
2.2	Amendment No. 1 to Acquisition Agreement, dated October 22, 1996, among Hi-Tiger International, Inc., AVTel Communications, Inc. and AVTel Holdings, Inc. (Incorporated by reference to Exhibit 2.2 to Registrant's Current Report on Form 8-K dated October 23, 1996).	
2.3	Stock Exchange Agreement, dated as of April 29, 1997, by and between the Registrant and Matrix Telecom, Inc. (Incorporated by reference to Exhibit 2 to Registrant's Current Report on Form 8-K dated April 30, 1997).	
2.4	Amendment to Stock Exchange Agreement, dated as of August 25, 1997, by and between the Registrant and Matrix Telecom, Inc. (Incorporated by reference to Exhibit 2 to Registrant's Current Report on Form 8-K dated August 25, 1997).	
2.5	Agreement and Plan of Merger, dated as of October 3, 1997, between AVTel Communications, Inc., a Delaware corporation and AVTel Communications, Inc., a Utah corporation. (Incorporated by reference to Exhibit 2.7 to Registrant's Annual Report on Form 10-KSB for the year ended September 30, 1997).	
2.6	Stock Purchase Agreement, dated as of July 22, 1998, among the Registrant and the shareholders of Remote Lojix/PCSI, Inc.	
2.7	First Amendment to Stock Purchase Agreement, dated as of August 18, 1998, among the Registrant and the shareholders of Remote Lojix/PCSI, Inc.	
2.8	Earnout Agreement, dated as of October 30, 1998, among the Registrant and certain shareholders of Remote Lojix/PCSI, Inc.	
3.1	Certificate of Incorporation of the Registrant. (Incorporated by reference to Exhibit 3.1 to Registrant's Annual Report on Form 10-KSB for the year ended September 30, 1997).	
3.2	Certificate of Designations, Preferences and Rights of Series B Convertible Preferred Stock.	
3.3	Bylaws of the Registrant. (Incorporated by reference to Exhibit 3.2 to Registrant's Annual Report on Form 10-KSB for the year ended September 30, 1997).	
10.1	Rights Agreements dated October 23, 1996, between the Registrant and holders of the Registrant's Series A Convertible Preferred Stock. (Incorporated by reference to Exhibit 4.2 to Registrant's Current Report on Form 8-K dated October 23, 1996).	
10.2	1997 Stock Incentive Plan. (Incorporated by reference to Exhibit A to the Registrant's definitive Proxy Statement on Schedule 14A dated January 8, 1997.)	

<u>Exhibit Number</u>	<u>Title of Document</u>	<u>Page Number</u>
10.3	1998 Stock Incentive Plan. (Incorporated by reference to Exhibit A to Registrant's definitive Proxy Statement on Schedule 14A dated April 28, 1998).	
10.4	New Best Connections, Inc. Amended and Restated 1997 Option Plan. (Incorporated by reference to Exhibit 4.2 to Registrant's Registration Statement on Form S-8 dated May 22, 1998).	
10.5	First Amendment to New Best Connections, Inc. Amended and Restated 1997 Option Plan.	
10.6	Registration Rights and Lockup Agreement dated December 1, 1997, between the Registrant and Matrix Telecom, Inc., on behalf of the stockholders of Matrix, (Incorporated by reference to Exhibit 4 to Registrant's Current Report on Form 8-K dated December 1, 1997).	
10.7	Triple Net Real Property Lease (Multi-Tenant Building) dated as of February 16, 1998, by and between Bath Street Partners, a California limited partnership and the Company. (Incorporated by reference to Exhibit 10.8 to Registrant's Annual Report on Form 10-K for the year ended December 31, 1997).	
10.8	Commercial Lease Agreement dated February 28, 1995, Matrix Telecom, Inc. and Ameritas Life Insurance Corp., as amended by Lease Modification Agreement dated March 2, 1995. (Incorporated by reference to Exhibit 10.9 to Registrant's Annual Report on Form 10-K for the year ended December 31, 1997).	
10.9	Resale Solutions Switched Services Agreement dated March 12, 1998, between Matrix Telecom, Inc. and Sprint Communications Company L.P. (Incorporated by reference to Exhibit 10.10 to Registrant's Annual Report on Form 10-K for the year ended December 31, 1997).	
10.10	Amendment to Carrier Transport Switched Services Agreement dated October 15, 1998, between Matrix Telecom and Sprint Communications Company L.P. (Incorporated by reference to Exhibit 10.1 to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1998).	
10.11	Loan and Security Agreement dated October 2, 1998, among Registrant, Matrix Telecom, Inc. and Coast Business Credit. (Incorporated by reference to Exhibit 10.2 to Registrant's Quarterly Report on Form 10-Q for the quarter ended September 30, 1998).	
10.12	License Agreement dated as of March 1, 1999, between Matrix Telecom, Inc. and Electronic Data Systems Corporation.	
10.13	Convertible Preferred Stock and Warrants Purchase Agreement dated as of April 5, 1999, among Registrant, AMRO International, S.A., Austinvest Anstalt Balzers, and Esquire Trade & Finance Inc.	
10.14	Registration Rights Agreement dated as of April 5, 1999, among Registrant, AMRO International, S.A., Austinvest Anstalt Balzers, and Esquire Trade & Finance Inc.	
10.15	Stock Purchase Warrants granted by Registrant to AMRO International, S.A., Austinvest Anstalt Balzers, and Esquire Trade & Finance Inc.	
21	List of Subsidiaries.	

<u>Exhibit Number</u>	<u>Title of Document</u>
23	Consent of KPMG LLP.
27	Financial Data Schedule.

Page
Number

EXHIBIT 4

Proposed Tariff

TITLE SHEET

NETLOJIX TELECOM, INC.

RESALE TELECOMMUNICATIONS SERVICES

This tariff contains the descriptions, regulations, and rates applicable to the furnishing of resold interexchange telecommunications services provided by NetLojix Telecom, Inc. ("Company") within the State of South Dakota. This tariff is on file with the South Dakota Public Utilities Commission and copies may be inspected, during normal business hours, at the Company's principal place of business, 501 Bath Street, Santa Barbara, CA 93101, telephone number 1-877-NETLOJIX.

Issued: November 23, 1999

Effective: November __, 1999

Issued by:

Michael D. Ussery
NetLojix Telecom, Inc.
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CHECK SHEET

All pages of this tariff are effective as of the date shown. Original and revised pages as named below comprise all changes from the original tariff and are currently in effect as of the date on the bottom of this page.

<u>Page</u>	<u>Revision</u>	<u>Page</u>	<u>Revision</u>	<u>Page</u>	<u>Revision</u>	<u>Page</u>	<u>Revision</u>
Title	Original	26	Original				
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2	Original	28	Original				
3	Original	29	Original				
4	Original	30	Original				
5	Original	31	Original				
6	Original						
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EXPLANATION OF SYMBOLS

Any tariff modification shall be marked in the right-hand margin of the replacing tariff sheet with symbols described to indicate the place, nature, and extent of the change in text.

- C To Signify Changed Regulation
- D Delete or Discontinue
- I Change Resulting In An Increase To A Customer's Bill
- M Moved from Another Tariff Location
- N New
- R Change Resulting In A Reduction To A Customer's Bill
- S Matter Appearing Elsewhere or Repeated for Clarification
- T Change In Text or Regulation But No Change In Rate or Charge

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TARIFF FORMAT

- A. **Sheet Numbering** - Sheet numbers appear in the upper right corner of the page. Sheets are numbered sequentially. However, new sheets are occasionally added to the tariff. When a new sheet is added between sheets already in effect, a decimal is added. For example, a new sheet added between sheets 14 and 15 would be 14.1.
- B. **Sheet Revision Numbers** - Revision numbers also appear in the upper right corner of each page. These numbers are used to determine the most current sheet version on file with the Commission. For example, the 4th revised Sheet 14 cancels the 3rd revised Sheet 14. Because of various suspension periods, deferrals, etc. the Commission follows in their tariff approval process, the most current sheet number on file with the Commission is not always the tariff page in effect.
- C. **Paragraph Numbering Sequence** - There are nine levels of paragraph coding. Each level of coding is subservient to its next higher level:
- 2.
 - 2.1.
 - 2.1.1.
 - 2.1.1.A.
 - 2.1.1.A.1.
 - 2.1.1.A.1.(a).
 - 2.1.1.A.1.(a).i.
 - 2.1.1.A.1.(a).i.(i).
 - 2.1.1.A.1.(a).i.(i).(1).
- D. **Check Sheets** - When a tariff filing is made with the Commission, an updated check sheet accompanies the tariff filing. The check sheet lists the sheets contained in the tariff, with a cross reference to the current revision number. When new pages are added, the check sheet is changed to reflect the revision. All revisions made in a given filing are designated by an asterisk (*). There will be no other symbols used on the check sheet if these are the only changes made to it (i.e., the format, etc. remains the same, just revised revision levels on some pages). The tariff user should refer to the latest check sheet to find out if a particular sheet is the most current on file with the Commission.

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TECHNICAL TERMS AND ABBREVIATIONS

Access Line - An arrangement which connects the customer's location to a NetLojix network switching center.

Account Code - A numeric code which enables a customer to identify individual users for administrative purposes.

Authorization Code - A numerical code, one or more of which may be assigned to a Subscriber, to enable Company to identify the origin of service User so it may rate and bill the call. All authorization codes shall be the sole property of Company and no Subscriber shall have any property or other right or interest in the use of any particular authorization code. Automatic numbering identification (ANI) may be used as or in connection with the authorization code.

Automatic Numbering Identification (ANI) - A type of signaling provided by a local exchange telephone company which automatically identifies the local exchange line from which a call originates.

Company or Company - NetLojix Telecom, Inc.

Calls - Telephone messages completed by customers or users.

Commission - Refers to the [INSERT STATE] Public Service Commission.

Common Company - A company or entity providing telecommunications services to the public.

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

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TECHNICAL TERMS AND ABBREVIATIONS (Cont'd)

Feature Group D (FGD) - The method of "+1" access available through the switched network of the local exchange utility. FGD is also known as equal access.

Holidays - NetLojix Telecom, Inc.'s recognized holidays are New Year's Day, Martin Luther King, Jr. Day, President's Day, Memorial Day, Independence Day, Labor Day, Columbus Day, Veteran's Day, Thanksgiving Day and Christmas Day.

NetLojix - NetLojix Telecom, Inc.

Tariff - The entire body of regulated rates, tolls, rentals, changes, classifications, rules, procedures, policies, etc. adopted and filed with the Commission by a telephone utility in fulfilling its role of telecommunications service. The term may also be used in reference to similar documents filed with state regulatory agencies.

Telecommunications - The transmission of voice communications or, subject to the transmission capabilities of the service, the transmission of data, facsimile, signaling, metering, or other similar communications.

User or End User - A Customer, Joint User, or any other person(s) authorized by a Customer to use service provided under this tariff.

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Section 1 – APPLICATION OF TARIFF

- 1.1 This tariff contains the regulations and rates applicable to resold intrastate interexchange telecommunications services provided by Company between one or more points within the State of [INSERT STATE]. Company's services are furnished subject to the availability of facilities and subject to the terms and conditions of this tariff.
- 1.2 The rates and regulations contained in this tariff apply only to the services furnished by Company and do not apply, unless otherwise specified, to the lines, facilities, or services provided by a local exchange telephone company or other common Company for use in accessing the services of Company.
- 1.3 The Subscriber is entitled to limit the use of Company's services by Users at the Subscriber's facilities, and may use other common Companies in addition to or in lieu of Company.
- 1.4 NetLojix will provide resold intrastate interexchange telecommunications services on a 24 hour basis. NetLojix maintains a highly qualified customer service staff accessible via a toll-free number. When applying for service each prospective customer will be required to furnish NetLojix with the following information:
- (a) Name of the party who will be responsible for payment for the interexchange service provided.
 - (b) Address or exact location of the premises where interexchange service is to be provided and billed.
- Service shall be considered initiated hereunder upon the earlier of the following:
- (a) First use by the customer of the NetLojix service, and,
 - (b) The receipt by NetLojix of a customer's initial payment for NetLojix service.
- 1.5 Service is provided and billed on the basis of usage except as otherwise specified beginning on the date that billing becomes effective, and continues to be provided after the initial period until the customer requests cancellation or until NetLojix disconnects service pursuant to the provisions of this Tariff.

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SECTION 2 – REGULATIONS**2.1 Undertaking of the Company****2.1.1 Scope**

Resold intrastate interexchange telecommunications is furnished in accordance with the conditions and regulations which are set forth in the body of this Tariff.

2.1.2 Limitations

- A. Service is offered subject to the availability of facilities as provided under this Tariff.
- B. NetLojix reserves the right to discontinue furnishing service, or limit the use of service necessitated by conditions beyond it's control; or when the customer is using service in violation of the law or the provisions of this Tariff.
- C. All facilities provided under this Tariff are controlled by NetLojix and the customer may not transfer or assign the use of service of facilities, except with the express written consent of the Company. Such transfer or assignment shall only apply where there is no interruption of the use or location of the service or facilities.
- D. Prior written permission from the Company is required before any assignment or transfer. All regulations and conditions contained in this Tariff shall apply to all such permitted assignees or transferees, as well as all conditions for service.

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SECTION 2 – REGULATIONS (Cont'd)

2.1 Undertaking of the Company (Cont'd)

2.1.3 Liability of the Company

- A. Except as otherwise stated in this section, the liability of Company for damages arising out of either: (1) the furnishing of its services, including but not limited to mistakes, omissions, interruptions, delays, or errors, or other defects, representations, or use of these services, or (2) the failure to furnish its service, whether caused by acts or omission, shall be limited to the extension of allowances to the Customer for interruptions in service as set forth in Section 2.1.5.
- B. Except for the extension of allowances to the Customer for interruptions in service as set forth in Section 2.1.5, Company shall not be liable to a Customer or third party for any direct, indirect, special, incidental, reliance, consequential, exemplary or punitive damages, including, but not limited to, loss of revenue or profits, for any reason whatsoever, including, but not limited to, any act or omission, failure to perform, delay, interruption, failure to provide any service or any failure in or breakdown of facilities associated with the service.
- C. The liability of Company for errors in billing that result in overpayment by the Customer shall be limited to a credit equal to the dollar amount erroneously billed or, in the event that payment has been made and service has been discontinued, to a refund of the amount erroneously billed.

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SECTION 2 – REGULATIONS (Cont'd)

2.1 Undertaking of the Company (Cont'd)

2.1.3 Liability of Company (Cont'd)

D. Company shall not be liable for any claims for loss or damages involving:

1. Any act or omission of: (1) the Customer, (2) any other entity furnishing service, equipment or facilities for use in conjunction with services or facilities provided by Company; or (3) common Companies or warehousemen;
2. Any delay or failure of performance or equipment due to causes beyond Company's control, including but not limited to, acts of God, fires, floods, earthquakes, hurricanes, or other catastrophes; national emergencies, insurrections, riots, wars or other civil commotions; strikes, lockouts, work stoppages or other labor difficulties; criminal action taken against Company; unavailability, failure or malfunction of equipment or facilities provided by the Customer or third parties; and any law, order, regulation or other action of any governing authority or agency thereof;
3. Any unlawful or unauthorized use of Company's facilities and services;
4. Libel, slander, invasion of privacy or infringement of patents, trade secrets, or copyrights arising from or in connection with the transmission of communications by means of Company-provided facilities or services; or by means of the combination of Company-provided facilities or services with Customer-provided facilities or services;

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SECTION 2 – REGULATIONS (Cont'd)

2.1 Undertaking of the Company (Cont'd)

2.1.3 Liability of Company (Cont'd)

- D. Company shall not be liable for any claims for loss or damages involving: (Cont'd)
5. Breach in the privacy or security of communications transmitted over Company's facilities;
 6. Changes in any of the facilities, operations or procedures of Company that render any equipment, facilities or services provided by the Customer obsolete, or require modification or alteration of such equipment, facilities or services, or otherwise affect their use or performance, except where reasonable notice is required by Company and is not provided to the Customer, in which event Company's liability is limited as set forth in section 2.1.3;
 7. Defacement of or damage to Customer premises resulting from the furnishing of services or equipment on such premises or the installation or removal thereof;
 8. Injury to property or injury or death to persons, including claims for payments made under Worker's Compensation law or under any plan for employee disability or death benefits, arising out of, or caused by, any act or omission of the Customer, or the construction, installation, maintenance, presence, use or removal of the Customer's facilities or equipment connected, or to be connected to Company's facilities;

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SECTION 2 – REGULATIONS (Cont'd)

2.1 Undertaking of the Company (Cont'd)

2.1.3 Liability of Company (Cont'd)

- D. Company shall not be liable for any claims for loss or damages involving: (Cont'd)**
- 9. Any intentional, wrongful act of a Company employee when such act is not within the scope of the employee's responsibilities for Company and/or is not authorized by Company;**
 - 10. Any representations made by Company employees that do not comport, or that are inconsistent, with the provisions of this Tariff;**
 - 11. Any act or omission in connection with the provision of 911, E911, or similar services involving emergencies;**
 - 12. Any noncompletion of calls due to network busy conditions;**
 - 13. Any calls not actually attempted to be completed during any period that service is unavailable.**

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SECTION 2 – REGULATIONS (Cont'd)**2.1 Undertaking of the Company (Cont'd)****2.1.3 Liability of Company (Cont'd)**

- E. Company shall be indemnified, defended and held harmless by the Customer or end user from and against any and all claims, loss, demands, suites, expense, or other action or any liability whatsoever, including attorney fees, whether suffered, made, instituted, or asserted by the Customer or by any other party, for any personal injury to or death or any person or persons, and for any loss, damage or destruction of any property, including environmental contamination, whether owned by the Customer or by any other party, caused or claimed to have been caused directly or indirectly by the installation, operation, failure to operate, maintenance, presence, condition, location, use or removal of any Company or customer equipment or facilities or service provided by Company.
- F. Company assumes no responsibility for the availability or performance of any cable or satellite systems or related facilities under the control of other entities, or for other facilities provided by other entities used for service to the Customer, even if Company has acted as the Customer's agent in arranging for such facilities or services. Such facilities are provided subject such degree of protection or nonpreemptibility as may be provided by the other entities.
- G. Any claim of whatever nature against Company shall be deemed conclusively to have been waived unless presented in writing to Company within thirty (30) days after the date of the occurrence that gave rise to the claim.
- H. Company MAKES NO WARRANTIES OR REPRESENTATIONS, EXPRESS OR IMPLIED EITHER IN FACT OR BY OPERATION OF LAW, STATUTORY OR OTHERWISE, INCLUDING WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR USE, EXCEPT THOSE EXPRESSLY SET FORTH HEREIN.

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SECTION 2 – REGULATIONS (Cont'd)**2.1 Undertaking of the Company (Cont'd)****2.1.4 Initial Service Periods and Termination of Service**

The initial service period is one (1) month except as specified in other sections of this Tariff. The initial service period of any class may be greater than that specified above, or elsewhere in this Tariff, when facilities are not available and the customer's location or the character or quantity of the service requested is such that, upon termination of the customer's user thereof, the required facilities are not likely to be useful as a part of a properly designed telephone distribution system serving telephone users in or beyond the customer's location.

2.1.5 Credit Allowances for Interruption of Service

Credit allowance for the interruption of service which is not due to the Company's testing or adjusting, negligence of the customer, or to the failure of channels or equipment provided by the customer, are subject to the general liability provisions set forth. It shall be the obligation of the customer to notify the Company immediately of any interruption in service for which a credit allowance is desired. Before giving such notice, the customer shall ascertain that the trouble is not being caused by any action or omission by the customer within his control, or is not in wiring or equipment, if any, furnished by the customer and connected to the Company's facilities.

The customer shall be credited for an interruption of more than twenty-four hours as follows:

Credit Formula:

$$\text{Credit} = A/B \times C$$

"A" - outage time in hours

"B" - total hours in a month (month = 720)

"C" - total monthly charge for affected facility

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SECTION 2 – REGULATIONS (Cont'd)**2.2 Responsibilities of the Subscriber**

- 2.2.1 The Subscriber is responsible for placing any necessary orders; for complying with tariff regulations; for the placement of any stickers or tent cards provided by Company or as required by law; and for assuring that Users comply with tariff regulations. The Subscriber shall ensure compliance with any applicable laws, regulations, orders or other requirements (as they exist from time to time) of any governmental entity relating to services provided or made available by the Subscriber to Users. The Subscriber is also responsible for the payment of charges for calls originated at the Subscriber's numbers which are not collect, third party, calling card, or credit card calls.
- 2.2.2 The Subscriber must pay Company for replacement or repair of damage to the equipment or facilities of Company caused by negligence or willful act of the Subscriber, Users, or other, by improper use of the services, or by use of equipment provided by the Subscriber, Users, or others.
- 2.2.3 The Subscriber must pay for the loss through theft of any Company equipment installed at Subscriber's premises.
- 2.2.4 The Subscriber shall indemnify and save Company harmless from all liability disclaimed by Company in this tariff, arising in connection with the provision of service by Company, and shall protect and defend Company from any suits or claims against Company and shall pay all expenses and satisfy all judgments rendered against Company in connection herewith. Company shall notify the Subscriber of any suite or claim against Company of which it is aware.

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SECTION 2 – REGULATIONS (Cont'd)**2.3 Use of Service**

The services tariffed are furnished subject to the condition that they will not be used for any unlawful purpose. Services will not be furnished if any law enforcement agency, acting within its jurisdiction, advises that such services are being used or are likely to be used in violation of the law.

2.4 Customer Equipment and Channels**2.4.1 Interconnection With Other Companies**

Service furnished by NetLojix may be connected with services or facilities of another participating Company or may be provided over facilities which are solely provided by local utilities and/or interexchange Companies other than NetLojix. Service furnished by NetLojix is not part of a joint undertaking with such other Companies.

2.5 Advance Payments and Deposits

NetLojix may require a Customer to make an advance payment before services and facilities are furnished. The advanced payment will not exceed an amount equal to two-month's estimated charges, as determined by NetLojix. The advance payment will be credited to the Customer's bill. An advance payment may be required in addition to a deposit.

2.5.1 Deposits

NetLojix may require a Customer to make a deposit to be held as a guarantee for payment of charges. A deposit does not relieve the Customer of the responsibility for prompt payment of bills on presentation. The deposit will not exceed an amount equal to:

- A. two month's charges for a service or facility which has a minimum payment period of one month; or

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SECTION 2 – REGULATIONS (Cont'd)

2.5 Advance Payments and Deposits (cont'd)

2.5.1 Deposits (cont'd)

- B. the charges that would apply for the minimum payment period for a service or facility which has a minimum payment period of more than one month; except that the deposit may include an additional amount in the event that a termination charge is applicable.

A deposit may be required in addition to an advance payment.

When a service or a facility is discontinued, the amount of a deposit, if any, will be applied to the Customer's account and any credit balance remaining will be refunded. Before the service or facility is discontinued, NetLojix may, at its option, return the deposit or credit it to the Customer's account.

Deposits held will accrue interest at a rate consistent with the South Dakota P.U.C. where the Customer is billed. Customers who present a credit risk may also be required, at any time, to provide other assurances of, or security for, the payment of NetLojix's charges for its services as deemed necessary, including without limitation, advance payments for service, third party guarantees or payment, pledges or other grants of security interests in the Customers' assets, and similar arrangements. The required deposits or other security may be increased or decreased by NetLojix, as it deems appropriate in the light of changing conditions.

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Fort Worth, TX 76180

SECTION 2 – REGULATIONS (Cont'd)**2.6 Rendering and Payment of Bills****2.6.1 Rendering of Bills**

Regular customer bills are issued monthly. Each bill contains the dates included in the billing period, dates for service charges associated with work performed and the last date for timely payment. Bills include the amount the customer is charged, stated by category, sales tax and excise tax, with separate entries for total amounts current or in arrears. Reasonable customer requested adjustments to monthly bills may be made if the Customer brings the desired adjustment to NetLojix's attention within sixty (60) days of issuance of the bill. NetLojix reserves the right to extend the period for adjustments beyond the sixty (60) day period if, in NetLojix's judgment, the situation so warrants.

2.6.2 Due Dates

Customer payments are considered prompt when received by NetLojix or its agent by the due date on the bill. The due date is thirty (30) days after the bill is rendered. Any Customer not paying within thirty (30) days is considered delinquent.

Issued: November 23, 1999

Effective: November __, 1999

Issued by:

Michael D. Ussery
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

SECTION 2 – REGULATIONS (Cont'd)**2.6 Rendering and Payment of Bills (Cont'd)****2.6.3 Payment for Service**

The rates specified in this tariff are rates based on usage, billed monthly and payable in arrears. All Customers shall be permitted to have a last date for timely payment changeable for cause in writing. Such a change will become effective when acknowledged by NetLojix. Until acknowledged, no change in date of timely payment is recognized by NetLojix. The maximum payment required for restoration of service that existed prior to disconnection shall be the total past-due amount, applicable charges and Advance Payment and Deposit as specified elsewhere in this tariff. The Customer is held responsible for all charges for services furnished at the Customer's request and for all toll service furnished. It is the Customer's responsibility to contact NetLojix when no bill is received. Except as provided elsewhere in this tariff, the rate for a full billing period is specified in this tariff. If the prorating indicates a refund is due, the refund is applied as a bill credit.

The Customer is liable for any legal fees incurred by NetLojix in the process of collecting a past-due amount. The amount of these fees can be determined by officers of court if the proceedings are fully litigated. If the Customer acquiesces to NetLojix's demand for payment before a judgment is rendered, NetLojix will bill the delinquent customer for costs incurred to that point. The Customer is entitled to a statement of legal fees that are being assessed.

2.6.4 Disputed Bills

In the event of a dispute concerning a bill, NetLojix may require the Customer to pay the undisputed portion of the bill. Following payment of the undisputed amount, efforts to resolve the complaint, using complaint procedures in this tariff, shall continue for no more than forty-five (45) days after the rendering of the disputed bill. During this period the service shall not be disconnected for nonpayment of the disputed amount.

Issued: November 23, 1999

Effective: November __, 1999

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SECTION 2 – REGULATIONS (Cont'd)**2.6 Rendering and Payment of Bills (Cont'd)****2.6.5 Customer Complaints**

Customer complaints are handled by a full service customer service department. A customer or prospective customer may initiate a complaint or billing inquiry with NetLojix by either calling 1-877-NETLOJIX during normal business hours or submitting a written complaint to:

NetLojix Telecom, Inc.
501 Bath Street
Santa Barbara, CA 93101

NetLojix's response to the customer will generally be in the same form used by the customer. However, NetLojix may respond to written complaints by telephone when it believes such communications will be more effective in resolution of the issue. When a complaint or billing inquiry is received, a NetLojix customer service representative will determine if the call was processed by NetLojix, and if so, the type of call. If it is a fraud or unanswered call for which the customer should not be held responsible, NetLojix will refund all charges for the call. If there is a rate dispute, NetLojix will adjust the charges if an error is confirmed. The customer may at any point during the resolution of the complaint or billing inquiry seek review by a NetLojix supervisor or manager. If the customer wishes further review after investigation and final resolution by NetLojix, the customer may direct all appropriate information to the Federal Communications Commission or the South Dakota Public Utilities Commission, located at 500 E. Capitol Avenue, State Capitol Building, Pierre, SD 57501, telephone number (605) 773-3201.

Issued: November 23, 1999**Effective: November __, 1999****Issued by:**

Michael D. Ussery
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

SECTION 2 – REGULATIONS (Cont'd)**2.6 Rendering and Payment of Bills (Cont'd)****2.6.6 Discontinuance of Service**

Company may terminate Service to a Customer for nonpayment of undisputed charges or other violation of this tariff or provision of law upon written notice, as required below, to the Customer without incurring any liability for damages due to loss of telephone Service to the Customer. Termination of Service will not occur on any Friday, Saturday, Sunday or legal holidays. Charges will not be considered past due until thirty (30) days from the closing date printed on the Customer's bill.

The Company may refuse or discontinue Service under the following conditions provided that the Customer shall be given five (5) days written notice, excluding Sundays and legal holidays, to comply with any rule or remedy any deficiency:

- A. For non-compliance with or violation of any State, municipal, or Federal law, ordinance or regulation pertaining to telephone Service, including, but not limited to, the placement of harassing, annoying or repeated unwanted calls of which the Company receives notice.
- B. For use of telephone Service for any purpose other than that described in the application.
- C. For neglect or refusal to provide reasonable access to the Company or its agents for the purpose of inspection and maintenance of equipment owned by the Company or its agents.
- D. For noncompliance with or violation of Commission regulation or the Company's rules and regulations on file with the Commission.

Issued: November 23, 1999

Effective: November __, 1999

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SECTION 2 – REGULATIONS (Cont'd)

2.6 Rendering and Payment of Bills (Cont'd)

2.6.6 Discontinuance of Service (Cont'd)

- E. For failure of Customer to pay a bill for utility service when due.
- F. For failure of Customer to meet the Company's credit requirements.
- G. Without notice in the event of Customer use of equipment or services in such a manner as to adversely affect the Company's equipment or Service to others.
- H. Without notice in the event of tampering with the equipment or services owned by the Company, the Underlying Company or their agents.
- I. Without notice in the event of a condition determined to be hazardous to the Customer, to other Customers of the Company, to the Company's equipment, the public, or to employees of the Company.

Issued: November 23, 1999

Effective: November __, 1999

Issued by:

Michael D. Ussery
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Fort Worth, TX 76180

SECTION 2 – REGULATIONS (Cont'd)**2.7 Taxes And Fees**

Now, or at any future time, if a state or municipality possesses or acquires the legal right to impose an occupation tax, license tax, sales tax, gross receipts tax, permit fee, franchise fee or other similar charge upon NetLojix, and has imposed, or imposes the same by ordinance or otherwise, such taxes, fees or charges shall be billed to the customers receiving service within the territorial limits of such municipality. Such billing shall allocate the tax, fee or charge among customers uniformly on the basis of each customer's monthly charges for the types of service made subject to such tax, fee or charge.

If at any future time a county or other local taxing authority acquires the legal right to impose an occupation tax, license tax, sales tax, gross receipts tax, permit fee, franchise fee or other similar charge upon NetLojix, and has imposed, or imposes the same by ordinance or otherwise, such taxes, fees or charges shall be billed to the customers receiving service within the territorial limits of such municipality. Such billing shall allocate the tax, fee or charge among customers uniformly on the basis of each customer's monthly charges for the types of service made to such tax, fee or charge.

Issued: November 23, 1999

Effective: November __, 1999

Issued by:

Michael D. Ussery
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

SECTION 3 – EXPLANATION OF RATES**3.1 Timing of Calls**

The Customer's long distance usage charge is based on the actual usage of NetLojix's network. Usage begins when the called party picks up the receiver. When the called party picks up, is determined by hardware answer supervision in which the local telephone company sends a signal to the switch or the software utilizing audio tone detection. A call is terminated when either calling party hangs up.

3.2 Uncompleted Call Crediting

If a Customer receives a bill for an uncompleted call, NetLojix will reimburse the customer for the full amount.

3.3 Minimum Call Completion Rate

A Customer can expect a call completion rate (number of calls completed/number of calls attempted) of not less than 95% during peak use periods for all FGD services.

3.4 Rates Based Upon Calculation of Distance

Usage charges for all mileage sensitive products are based on the airline distance between rate centers associated with the originating and terminating points of the call.

The airline mileage between rate centers is determined by applying the formula below to the vertical and horizontal coordinates associated with the rate centers involved. The Company uses the rate centers that are produced by Bell Communications Research in the NPA-NXX V & H Coordinates Tape and Bell's NECA Tariff No. 4.

FORMULA: The square
 root of:
$$\frac{(V1 - V2)^2 + (H1 - H2)^2}{10}$$

Issued: November 23, 1999

Effective: November __, 1999

Issued by:

Michael D. Ussery
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

SECTION 4 – SERVICE OFFERINGS**4.1 Long Distance Service**

Company's Long Distance Service (LDS) is a communications service which is available for use by customers twenty-four (24) hours a day. Customers may originate LDS from locations served by the Carrier, and may terminate in all locations within the State of South Dakota.

The service is offered in Feature Group D (FGD) exchanges where the Customer's local telephone lines are presubscribed by the local exchange company to the Company's LDS service, such that "1+" interLATA calls are automatically routed to the Company's network.

4.2 Toll Free Service

Toll Free Service is an inbound communications service which permits calls to be completed at the Customer's location without charge to the calling party. Access to the service is gained by dialing a ten (10) digit telephone number (800+ NXX-XXXX) which will terminate at the Customer's location. Calls may originate from any location within the State of South Dakota and may terminate at the Customer's location.

Toll Free Service will be billed per call based on the duration of the call. Usage discounts apply to aggregate monthly interstate and intrastate usage.

Toll Free service calls are originated via normal shared use facilities and are terminated via the Customer's local exchange service access line.

Issued: November 23, 1999**Effective: November __, 1999****Issued by:**

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Fort Worth, TX 76180

SECTION 4 – SERVICE OFFERINGS (Cont'd)

4.3 Miscellaneous Services

RESERVED FOR FUTURE USE

Issued: November 23, 1999

Effective: November __, 1999

Issued by:

Michael D. Ussery
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

SECTION 5 - RATES

5.1 Long Distance Service

Rate Per Minute

24 hours a day, 7 days a week,
365 days a year

\$.30

5.2 Toll Free Service

Rate Per Minute

24 hours a day, 7 days a week,
365 days a year

\$.30

5.3 Miscellaneous Services

RESERVED FOR FUTURE USE

Issued: November 23, 1999

Effective: November __, 1999

Issued by:

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NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

SECTION 5 – RATES

5.4 Late Payment Charge

Interest charges of 1.5% per month will be assessed on all unpaid balances more than thirty days old.

5.5 Return Check Charge

A return check charge of \$25.00 will be assessed for checks returned for insufficient funds.

5.6 Restoration of Service

A restoration fee of \$25.00 per occurrence is charged when service is re-established for customers who had been disconnected for non-payment.

5.7 Directory Assistance Charge

Company will connect LDS Service Customers to Directory Assistance (DA) for a fee of \$0.75 per occurrence.

5.8 Special Promotions

The Company will, from time to time, offer special promotions to its customers waiving certain charges. These promotions will be approved by the Commission with specific starting and ending dates.

5.9 Payphone Surcharge

A charge will apply to calls that originate from any payphone used to access Company's services.

Rate per Call: \$0.24

Issued: November 23, 1999

Effective: November __, 1999

Issued by:

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8721 Airport Freeway
Fort Worth, TX 76180

SECTION 5 – RATES

5.10 Special Rates For The Handicapped

5.10.1 Directory Assistance

There shall be no charge for up to fifty (50) calls per billing cycle from lines or trunks serving individuals with disabilities. Company shall charge the prevailing tariff rates for every call in excess of fifty (50) calls within a billing cycle.

5.10.2 Hearing and Speech Impaired Persons

Intrastate toll message rates for TDD users shall be evening rates for daytime calls and night rates for evening and night calls.

5.10.3 Telecommunications Relay Service

The charge for intrastate toll calls received from the relay service, will be 50% percent off of the otherwise applicable rate for a voice nonrelay call except that where either the calling or called party indicates that either party is both hearing and visually impaired, the call shall be discounted 60 percent off of the otherwise applicable rate for a voice nonrelay call. The above discounts apply only to time-sensitive elements of a charge for the call and shall not apply to per call charges such as a credit card surcharge.

307668.1

Issued: November 23, 1999

Effective: November __, 1999

Issued by:

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Fort Worth, TX 76180

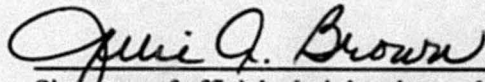
VERIFICATION

VERIFICATION

I, James P. Pisani, declare under penalty of perjury that I am authorized to make this verification on behalf of NetLojix Telecom, Inc., the Applicant in the subject proceeding, that I have read the foregoing information and know the contents thereof; that the same are true of my knowledge, except as to matters which are therein stated on information or belief, and as to those matters I believe to be true.


James P. Pisani
President
NetLojix Telecom, Inc.

Sworn and subscribed before me this 18 day of Oct 1999.


Signature of official administering oath

My commission expires: 7/26/2001



ORIGINAL DOCUMENT IS PRINTED ON CHEMICAL RESISTANT PAPER WITH A MICROPRINTED BORDER

SWIDLER BERLIN SHEREFF FRIEDMAN, LLP

3000 K STREET, N.W. SUITE 300
WASHINGTON, DC 20007

CHECK DATE

11/22/99

CHECK NO. D 117416

Citibank DC Operating
1775 Pennsylvania Avenue, NW
Suite 440
Washington, DC 20006

CHECK AMOUNT

250.00*****

TWO HUNDRED FIFTY AND 00/100 Dollars

TWO SIGNATURES REQUIRED ON CHECK
OVER \$10,000.00

PAY
TO THE
ORDER OF

South Dakota Public
Utilities Commission

OPERATING ACCOUNT

THE REVERSE SIDE OF THIS DOCUMENT INCLUDES AN ARTIFICIAL WATERMARK. HOLD AT AN ANGLE TO VIEW.

⑈117416⑈ ⑆254070116⑆ ⑆37402064⑈

South Dakota Public Utilities Commission

WEEKLY FILINGS

For the Period of November 18, 1999 through November 24, 1999

If you need a complete copy of a filing faxed, overnight expressed, or mailed to you, please contact Delaine Kolbo within five business days of this filing.

Phone: 605-773-3705 Fax: 605-773-3809

CONSUMER COMPLAINTS

CT99-059 In the Matter of the Complaint filed by Nancy Van Heerde, Sioux Falls, South Dakota, against The Furst Group Regarding Unauthorized Switching of Services.

On November 18, 1999, the Commission received a formal complaint from Nancy Van Heerde indicating that Ms. Van Heerde's long distance service had been switched to Furst Group by a deceptive telemarketer. Furst Group has issued a partial credit for an error concerning the Complainant's address. Furst Group has provided a tape of the verification conversation. The Complainant is not satisfied with the offered resolution and has requested further consideration by the Commission.

Staff Analyst: Leni Healy
Staff Attorney: Camron Hoseck
Date Filed: 11/18/99
Intervention Deadline: NA

CT99-060 In the Matter of the Complaint filed by Rueben W. Hoffmann, Aberdeen, South Dakota, against OLS, Inc. Regarding Unauthorized Switching of Services.

The Complainant indicates that he received a call from a telemarketer claiming to be with AT&T who wanted to combine his billing. As a result he received a billing from OLS. The Complainant is requesting removal of all charges and \$1000.

Staff Analyst: Leni Healy
Staff Attorney: Camron Hoseck
Date Filed: 11/19/99
Intervention Date: NA

CT99-061 In the Matter of the Complaint filed by Normajean Johnson, Vermillion, South Dakota, against OLS, Inc. Regarding Unauthorized Switching of Services.

The Complainant claims that her long distance service was with Promise Net. When she received her billing, she was billed by OLS, Inc. at a higher rate.

Staff Analyst: Leni Healy
Staff Attorney: Karen Cremer
Date Filed: 11/22/99
Intervention Date: NA

CT99-062 In the Matter of the Complaint filed by Marilyn Crompton, Aberdeen, South Dakota, against OLS, Inc. Regarding Unauthorized Switching of Services.

The Complainants indicate that a telemarketer representing U S WEST called her concerning her billing. As a result of this conversation, her service was switched to OLS, Inc. The Complainant requests that a large fine should be assessed to OLS for this activity.

Staff Analyst: Leni Healy
Staff Attorney: Karen Cremer
Date Filed: 11/22/99
Intervention Deadline: NA

CT99-063 In the Matter of the Complaint filed by Allen and Joyce Beckler, Aberdeen, South Dakota, against OLS, Inc. Regarding Switching of Services through Deceptive Telemarketing Practices.

The Complainants indicate that a telemarketer contacted them indicating that she was with U S WEST contacting them about billing issues. As a result of the call, their service was switched to OLS, Inc. The Complainants request that all assessed charges be dropped and that \$1000 in penalties be paid to them.

Staff Analyst: Leni Healy
Staff Attorney: Karen Cremer
Date Filed: 11/22/99
Intervention Date: NA

TELECOMMUNICATIONS

TC99-106 In the Matter of the Establishment of Different Rates for Interconnection and Unbundled Network Elements in at Least Three Geographic Areas.

In August of 1996, the Federal Communications Commission (FCC) issued its Local Competition Order implementing section 251 of the federal Telecommunications Act of

1996. Section 51.507(f) required each state commission to establish different rates for interconnection and unbundled network elements (UNEs) in at least three geographic areas within the state to reflect geographic cost differences. The Eighth Circuit subsequently stayed and then vacated the deaveraging rule. Based on those decisions, the Commission did not establish different rates for different geographic areas. However, in January of 1999, the U. S. Supreme Court reversed the Eighth Circuit's decision. On May 7, 1999, the FCC stayed the effectiveness of the rule in order to allow states additional time to comply with the rule. By order released November 2, 1999, the FCC ruled that the stay will be lifted on May 1, 2000. In the Matter of the Federal-State Joint Board on Universal Service, CC Docket 96-45, Ninth Report and Order and Eighteenth Order on Reconsideration, FCC 99-306, paragraph 120 (rel. Nov. 2, 1999). The order provides that by May 1, 2000, "states are required to establish different rates for interconnection and UNEs in at least three geographic areas pursuant to section 51.507(f) of the Commission's rules." Id. At its November 15, 1999, meeting, the Public Utilities Commission (Commission) considered how to proceed in this matter. After listening to comments from interested persons, the Commission decided to request written comments on how to proceed from interested persons or entities. On or before December 17, 1999, interested persons or entities may file written comments on how the Commission should establish different rates for interconnection and UNEs in at least three geographic areas within the state to reflect geographic cost differences. The Commission is interested in comments on whether the Commission may comply with the FCC's order to establish different rates for interconnection and UNEs in at least three geographic areas through a rulemaking or whether different rates must be established for specific companies in contested case dockets. Interested persons or entities may submit proposed rules along with their comments.

Staff Analyst: Harlan Best

Staff Attorney: Karen Cremer and Camron Hoseck

Date Opened: 11/19/99

Written Comments Due: On or before 12/17/99

TC99-107 In the Matter of the Consideration of the Assessment of Fines and Other Penalties against Western Telecom; In the Matter of the Consideration of the Assessment of Fines and Other Penalties against Touchtone Communications.

At its November 15, 1999, meeting, the Commission voted to issue Orders to Show Cause against Western Telecom and Touchtone Communications as to why Western Telecom and Touchtone Communication should not be assessed civil fines or other penalties for violations of South Dakota laws. The Commission also ordered the company to submit a complete listing of South Dakota customers.

Staff Analyst: Leni Healy

Staff Attorneys: Camron Hoseck and Karen Cremer

Date Filed: 11/22/99
Intervention Deadline: 12/10/99

TC99-108 In the Matter of the Application of NetLojix Telecom, Inc. for a Certificate of Authority to Provide Telecommunications Services in South Dakota.

NetLojix Telecom, Inc. has filed a request for a Certificate of Authority to operate as a reseller of intrastate interexchange telecommunications services in South Dakota. NetLojix Telecom intends to offer direct dialed 1+ service, inbound/outbound message telecommunications service, switched and dedicated services, toll free service and post-paid calling service to and from all points within the State of South Dakota.

Staff Analyst: Michele Farris
Staff Attorney: Camron Hoseck
Date Filed: 11/23/99
Intervention Date: 12/10/99

TC99-109 In the Matter of the Filing for Approval of an Interconnection Agreement between U S WEST Communications, Inc. and New Edge Network, Inc. dba New Edge Networks.

On November 23, 1999, the Public Utilities Commission received an interconnection agreement between New Edge Network, Inc. d/b/a New Edge Networks and U S WEST Communications, Inc. for approval by the Commission. The agreement governs services for resale and certain unbundled network elements, ancillary functions and additional features (collectively referred to as "Network Elements") for New Edge Networks' offering and provisioning of telecommunications services. The agreement addresses interconnection and reciprocal compensation for the exchange of local traffic.

Any party wishing to comment on the agreement may do so by filing written comment with the Commission and the parties to the agreement no later than December 17, 1999. Parties to the agreement may file written responses to the comments no later than December 27, 1999.

Staff Attorney: Camron Hoseck
Date Filed: 11/23/99
Comments Due: 12/17/99

...

You may receive this listing and other PUC publications via our website or via internet e-mail. You may subscribe or unsubscribe to the PUC mailing lists at <http://www.state.sd.us/puc/>

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405 LEXINGTON AVENUE
NEW YORK, NY 10174
TELEPHONE (212) 973-0111
FACSIMILE (212) 891-9598

December 16, 1999

BY OVERNIGHT DELIVERY

Michele M. Farris, Utility Analyst
South Dakota Public Utilities Commission
State Capitol Building, 500 E. Capitol Ave.
Pierre, South Dakota 57501-5070

RECEIVED

DEC 17 1999

**SOUTH DAKOTA PUBLIC
UTILITIES COMMISSION**

Re: Responses to Data Request 1; Application of NetLojix Telecom, Inc. for a Certificate of Authority to Provide Resold Interexchange Telecommunication Services in South Dakota; Docket No. TC99-108

Dear Ms. Farris:

Please find below responses on behalf of NetLojix Telecom, Inc. ("NetLojix"), the applicant in the above-referenced proceeding, to your letter of December 6, 1999:

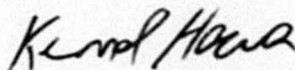
1. The email address of the representative to whom all inquiries must be made regarding complaints and regulatory matters (Question 9 in the application) is: mussery@netlojix.com
2. NetLojix is currently in its start-up phase and does not possess its own financial statements. Therefore, simultaneously with this filing, NetLojix is submitting a written waiver of S.D. Admin. R. 20:10:24:02(8).
3. NetLojix does not intend to collect deposits or advance payments. Accordingly, NetLojix has deleted all reference to deposits and advance payments from its tariff.
4. NetLojix does not intend to engage in multilevel marketing.
5. Enclosed is the original and one (1) copy of the substitute tariff to **replace** the tariff filed on November 23, 1999 as part of the application referenced above. The following revisions were made to the tariff pursuant to your instructions:

- a) Section 2.6 of the original tariff, referencing deposits and advance payments, has been revised to reflect that NetLojix will not be collecting deposits and advance payments at this time;
- b) The statement found in NetLojix's tariff format B, "Because of various suspension periods, deferrals, etc. the Commission follows in their tariff approval process, the most current sheet number on file with the Commission is not always the tariff page in effect." has been deleted;
- c) In the technical terms and abbreviations section of the tariff South Dakota has been inserted in the definition for Commission, for clarification "Company or Company" has been changed to "Company," and the errors in the definition of Feature Group D have been corrected;
- d) In Section 1 Application of Tariff, South Dakota has been inserted in 1.1;
- e) In Section 1.4 of the tariff, "service shall be considered initiated hereunder upon the earlier of the following," which indicates (a) or (b) has been revised accordingly;
- f) Sections 2.1.3.A, 2.1.3.B, 2.1.3.D.1(3), 2.1.3.D.7, 2.1.3.D.9, 2.1.3.D.10, 2.1.3.D.11, 2.1.3.E, and 2.1.3.G have been deleted from the tariff;
- g) Section 2.6.1 of the tariff requiring customers to notify NetLojix of any desired adjustments to their bill has been revised to allow the customer one-hundred eighty (180) days to dispute an invoice;
- h) Section 2.6.4 of the tariff has been revised to contain an explanation of what happens if a complaint has not been resolved in forty-five (45) days;
- i) The numbers 800-332-1782 and TTY Through Relay South Dakota 800-877-1113 have been add to the Commission address in Section 2.6.5 of the tariff.

Michele M. Farris
Utility Analyst
December 16, 1999
Page 3

Please date-stamp the enclosed extra copy of this letter and return it in the attached postage-paid envelope. If you have any further questions or concerns regarding NetLojix's application, please do not hesitate to contact Megan Rha or James Ferguson at (202) 424-7500.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "Kemal Hawa".

Kemal M. Hawa

Counsel for NetLojix Telecom, Inc.

Enclosures

cc: Craig Clark
Ernest Gillespie

TITLE SHEET

NETLOJIX TELECOM, INC.

RESALE TELECOMMUNICATIONS SERVICES

This tariff contains the descriptions, regulations, and rates applicable to the furnishing of resold interexchange telecommunications services provided by NetLojix Telecom, Inc. ("Company") within the State of South Dakota. This tariff is on file with the South Dakota Public Utilities Commission and copies may be inspected, during normal business hours, at the Company's principal place of business, 501 Bath Street, Santa Barbara, CA 93101, telephone number 1-877-NETLOJIX.

Issued: November 23, 1999

Effective:

Issued by:

Michael D. Ussery
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

CHECK SHEET

All pages of this tariff are effective as of the date shown. Original and revised pages as named below comprise all changes from the original tariff and are currently in effect as of the date on the bottom of this page.

<u>Page</u>	<u>Revision</u>	<u>Page</u>	<u>Revision</u>	<u>Page</u>	<u>Revision</u>	<u>Page</u>	<u>Revision</u>
Title	Original	26	Original				
1	Original	27	Original				
2	Original	28	Original				
3	Original						
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Issued: November 23, 1999

Effective:

Issued by:

Michael D. Ussery
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

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Issued: November 23, 1999

Effective:

Issued by:

Michael D. Ussery
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EXPLANATION OF SYMBOLS

Any tariff modification shall be marked in the right-hand margin of the replacing tariff sheet with symbols described to indicate the place, nature, and extent of the change in text.

- C To Signify Changed Regulation
- D Delete or Discontinue
- I Change Resulting In An Increase To A Customer's Bill
- M Moved from Another Tariff Location
- N New
- R Change Resulting In A Reduction To A Customer's Bill
- S Matter Appearing Elsewhere or Repeated for Clarification
- T Change In Text or Regulation But No Change In Rate or Charge

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TARIFF FORMAT

- A. Sheet Numbering - Sheet numbers appear in the upper right corner of the page. Sheets are numbered sequentially. However, new sheets are occasionally added to the tariff. When a new sheet is added between sheets already in effect, a decimal is added. For example, a new sheet added between sheets 14 and 15 would be 14.1.
- B. Sheet Revision Numbers - Revision numbers also appear in the upper right corner of each page. These numbers are used to determine the most current sheet version on file with the Commission. For example, the 4th revised Sheet 14 cancels the 3rd revised Sheet 14.
- C. Paragraph Numbering Sequence - There are nine levels of paragraph coding. Each level of coding is subservient to its next higher level:
- 2.
 - 2.1.
 - 2.1.1.
 - 2.1.1.A.
 - 2.1.1.A.1.
 - 2.1.1.A.1.(a).
 - 2.1.1.A.1.(a).I.
 - 2.1.1.A.1.(a).I.(i).
 - 2.1.1.A.1.(a).I.(i).(1).
- D. Check Sheets - When a tariff filing is made with the Commission, an updated check sheet accompanies the tariff filing. The check sheet lists the sheets contained in the tariff, with a cross reference to the current revision number. When new pages are added, the check sheet is changed to reflect the revision. All revisions made in a given filing are designated by an asterisk (*). There will be no other symbols used on the check sheet if these are the only changes made to it (i.e., the format, etc. remains the same, just revised revision levels on some pages). The tariff user should refer to the latest check sheet to find out if a particular sheet is the most current on file with the Commission.

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TECHNICAL TERMS AND ABBREVIATIONS

Access Line - An arrangement which connects the customer's location to a NetLojix network switching center.

Account Code - A numeric code which enables a customer to identify individual users for administrative purposes.

Authorization Code - A numerical code, one or more of which may be assigned to a Subscriber, to enable Company to identify the origin of service User so it may rate and bill the call. All authorization codes shall be the sole property of Company and no Subscriber shall have any property or other right or interest in the use of any particular authorization code. Automatic numbering identification (ANI) may be used as or in connection with the authorization code.

Automatic Numbering Identification (ANI) - A type of signaling provided by a local exchange telephone company which automatically identifies the local exchange line from which a call originates.

Company - NetLojix Telecom, Inc.

Calls - Telephone messages completed by customers or users.

Commission - Refers to the South Dakota Public Utilities Commission.

Common Company - A company or entity providing telecommunications services to the public.

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

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TECHNICAL TERMS AND ABBREVIATIONS (Cont'd)

Feature Group D (FGD) - The method of "+1" access available through the switched network of the local exchange utility. FGD is also known as equal access.

Holidays - NetLojix Telecom, Inc.'s recognized holidays are New Year's Day, Martin Luther King, Jr. Day, President's Day, Memorial Day, Independence Day, Labor Day, Columbus Day, Veteran's Day, Thanksgiving Day and Christmas Day.

NetLojix - NetLojix Telecom, Inc.

Tariff - The entire body of regulated rates, tolls, rentals, changes, classifications, rules, procedures, policies, etc. adopted and filed with the Commission by a telephone utility in fulfilling its role of telecommunications service. The term may also be used in reference to similar documents filed with state regulatory agencies.

Telecommunications - The transmission of voice communications or, subject to the transmission capabilities of the service, the transmission of data, facsimile, signaling, metering, or other similar communications.

User or End User - A Customer, Joint User, or any other person(s) authorized by a Customer to use service provided under this tariff.

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Section 1 – APPLICATION OF TARIFF

- 1.1 This tariff contains the regulations and rates applicable to resold intrastate interexchange telecommunications services provided by Company between one or more points within the State of South Dakota. Company's services are furnished subject to the availability of facilities and subject to the terms and conditions of this tariff.
- 1.2 The rates and regulations contained in this tariff apply only to the services furnished by Company and do not apply, unless otherwise specified, to the lines, facilities, or services provided by a local exchange telephone company or other common Company for use in accessing the services of Company.
- 1.3 The Subscriber is entitled to limit the use of Company's services by Users at the Subscriber's facilities, and may use other common Companies in addition to or in lieu of Company.
- 1.4 NetLojix will provide resold intrastate interexchange telecommunications services on a 24 hour basis. NetLojix maintains a highly qualified customer service staff accessible via a toll-free number. When applying for service each prospective customer will be required to furnish NetLojix with the following information:
- (a) Name of the party who will be responsible for payment for the interexchange service provided.
 - (b) Address or exact location of the premises where interexchange service is to be provided and billed.
- Service shall be considered initiated hereunder upon the earlier of the following:
- (a) First use by the customer of the NetLojix service, or,
 - (b) The receipt by NetLojix of a customer's initial payment for NetLojix service.
- 1.5 Service is provided and billed on the basis of usage except as otherwise specified beginning on the date that billing becomes effective, and continues to be provided after the initial period until the customer requests cancellation or until NetLojix disconnects service pursuant to the provisions of this Tariff.

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SECTION 2 – REGULATIONS

2.1 Undertaking of the Company

2.1.1 Scope

Resold intrastate interexchange telecommunications is furnished in accordance with the conditions and regulations which are set forth in the body of this Tariff.

2.1.2 Limitations

- A. Service is offered subject to the availability of facilities as provided under this Tariff.
- B. NetLojix reserves the right to discontinue furnishing service, or limit the use of service necessitated by conditions beyond it's control; or when the customer is using service in violation of the law or the provisions of this Tariff.
- C. All facilities provided under this Tariff are controlled by NetLojix and the customer may not transfer or assign the use of service of facilities, except with the express written consent of the Company. Such transfer or assignment shall only apply where there is no interruption of the use or location of the service or facilities.
- D. Prior written permission from the Company is required before any assignment or transfer. All regulations and conditions contained in this Tariff shall apply to all such permitted assignees or transferees, as well as all conditions for service.

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SECTION 2 – REGULATIONS (Cont'd)

2.1 Undertaking of the Company (Cont'd)

2.1.3 Liability of the Company

- A. The liability of Company for errors in billing that result in overpayment by the Customer shall be limited to a credit equal to the dollar amount erroneously billed or, in the event that payment has been made and service has been discontinued, to a refund of the amount erroneously billed.
- B. Company shall not be liable for any claims for loss or damages involving:
 - 1. Any act or omission of: (1) the Customer, or (2) any other entity furnishing service, equipment or facilities for use in conjunction with services or facilities provided by Company;
 - 2. Any delay or failure of performance or equipment due to causes beyond Company's control, including but not limited to, acts of God, fires, floods, earthquakes, hurricanes, or other catastrophes; national emergencies, insurrections, riots, wars or other civil commotions; strikes, lockouts, work stoppages or other labor difficulties; criminal action taken against Company; unavailability, failure or malfunction of equipment or facilities provided by the Customer or third parties; and any law, order, regulation or other action of any governing authority or agency thereof;
 - 3. Any unlawful or unauthorized use of Company's facilities and services;

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SECTION 2 – REGULATIONS (Cont'd)

2.1 Undertaking of the Company (Cont'd)

2.1.3 Liability of Company (Cont'd)

- B. Company shall not be liable for any claims for loss or damages involving: (Cont'd)
4. Libel, slander, invasion of privacy or infringement of patents, trade secrets, or copyrights arising from or in connection with the transmission of communications by means of Company-provided facilities or services; or by means of the combination of Company-provided facilities or services with Customer-provided facilities or services;
 5. Breach in the privacy or security of communications transmitted over Company's facilities;
 6. Changes in any of the facilities, operations or procedures of Company that render any equipment, facilities or services provided by the Customer obsolete, or require modification or alteration of such equipment, facilities or services, or otherwise affect their use or performance, except where reasonable notice is required by Company and is not provided to the Customer, in which event Company's liability is limited as set forth in section 2.1.3;
 7. Injury to property or injury or death to persons, including claims for payments made under Worker's Compensation law or under any plan for employee disability or death benefits, arising out of, or caused by, any act or omission of the Customer, or the construction, installation, maintenance, presence, use or removal of the Customer's facilities or equipment connected, or to be connected to Company's facilities;

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SECTION 2 – REGULATIONS (Cont'd)

2.1 Undertaking of the Company (Cont'd)

2.1.3 Liability of Company (Cont'd)

- B. Company shall not be liable for any claims for loss or damages involving: (Cont'd)
 - 8. Any noncompletion of calls due to network busy conditions;
 - 9. Any calls not actually attempted to be completed during any period that service is unavailable.
- C. Company assumes no responsibility for the availability or performance of any cable or satellite systems or related facilities under the control of other entities, or for other facilities provided by other entities used for service to the Customer, even if Company has acted as the Customer's agent in arranging for such facilities or services. Such facilities are provided subject such degree of protection or nonpreemptibility as may be provided by the other entities.
- D. COMPANY MAKES NO WARRANTIES OR REPRESENTATIONS, EXPRESS OR IMPLIED EITHER IN FACT OR BY OPERATION OF LAW, STATUTORY OR OTHERWISE, INCLUDING WARRANTIES OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR USE, EXCEPT THOSE EXPRESSLY SET FORTH HEREIN.

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SECTION 2 – REGULATIONS (Cont'd)**2.1 Undertaking of the Company (Cont'd)****2.1.4 Initial Service Periods and Termination of Service**

The initial service period is one (1) month except as specified in other sections of this Tariff. The initial service period of any class may be greater than that specified above, or elsewhere in this Tariff, when facilities are not available and the customer's location or the character or quantity of the service requested is such that, upon termination of the customer's user thereof, the required facilities are not likely to be useful as a part of a properly designed telephone distribution system serving telephone users in or beyond the customer's location.

2.1.5 Credit Allowances for Interruption of Service

Credit allowance for the interruption of service which is not due to the Company's testing or adjusting, negligence of the customer, or to the failure of channels or equipment provided by the customer, are subject to the general liability provisions set forth. It shall be the obligation of the customer to notify the Company immediately of any interruption in service for which a credit allowance is desired. Before giving such notice, the customer shall ascertain that the trouble is not being caused by any action or omission by the customer within his control, or is not in wiring or equipment, if any, furnished by the customer and connected to the Company's facilities.

The customer shall be credited for an interruption of more than twenty-four hours as follows:

Credit Formula:

Credit = A/B x C

"A" - outage time in hours

"B" - total hours in a month (month = 720)

"C" - total monthly charge for affected facility

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SECTION 2 – REGULATIONS (Cont'd)**2.2 Responsibilities of the Subscriber**

- 2.2.1 The Subscriber is responsible for placing any necessary orders; for complying with tariff regulations; for the placement of any stickers or tent cards provided by Company or as required by law; and for assuring that Users comply with tariff regulations. The Subscriber shall ensure compliance with any applicable laws, regulations, orders or other requirements (as they exist from time to time) of any governmental entity relating to services provided or made available by the Subscriber to Users. The Subscriber is also responsible for the payment of charges for calls originated at the Subscriber's numbers which are not collect, third party, calling card, or credit card calls.
- 2.2.2 The Subscriber must pay Company for replacement or repair of damage to the equipment or facilities of Company caused by negligence or willful act of the Subscriber, Users, or other, by improper use of the services, or by use of equipment provided by the Subscriber, Users, or others.
- 2.2.3 The Subscriber must pay for the loss through theft of any Company equipment installed at Subscriber's premises.
- 2.2.4 The Subscriber shall indemnify and save Company harmless from all liability disclaimed by Company in this tariff, arising in connection with the provision of service by Company, and shall protect and defend Company from any suits or claims against Company and shall pay all expenses and satisfy all judgments rendered against Company in connection herewith. Company shall notify the Subscriber of any suite or claim against Company of which it is aware.

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SECTION 2 – REGULATIONS (Cont'd)**2.3 Use of Service**

The services tariffed are furnished subject to the condition that they will not be used for any unlawful purpose. Services will not be furnished if any law enforcement agency, acting within its jurisdiction, advises that such services are being used or are likely to be used in violation of the law.

2.4 Customer Equipment and Channels**2.4.1 Interconnection With Other Companies**

Service furnished by NetLojix may be connected with services or facilities of another participating Company or may be provided over facilities which are solely provided by local utilities and/or interexchange Companies other than NetLojix. Service furnished by NetLojix is not part of a joint undertaking with such other Companies.

2.5 Advance Payments and Deposits

NetLojix will not collect advance payments or deposits from Customers.

2.6 Rendering and Payment of Bills**2.6.1 Rendering of Bills**

Regular customer bills are issued monthly. Each bill contains the dates included in the billing period, dates for service charges associated with work performed and the last date for timely payment. Bills include the amount the customer is charged, stated by category, sales tax and excise tax, with separate entries for total amounts current or in arrears. Reasonable customer requested adjustments to monthly bills may be made if the Customer brings the desired adjustment to NetLojix's attention within one-hundred eighty days (180) days of issuance of the bill. NetLojix reserves the right to extend the period for adjustments beyond the one-hundred eighty (180) day period if, in NetLojix's judgment, the situation so warrants.

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SECTION 2 – REGULATIONS (Cont'd)**2.6 Rendering and Payment of Bills (Cont'd)****2.6.2 Due Dates**

Customer payments are considered prompt when received by NetLojix or its agent by the due date on the bill. The due date is thirty (30) days after the bill is rendered. Any Customer not paying within thirty (30) days is considered delinquent.

2.6.3 Payment for Service

The rates specified in this tariff are rates based on usage, billed monthly and payable in arrears. All Customers shall be permitted to have a last date for timely payment changeable for cause in writing. Such a change will become effective when acknowledged by NetLojix. Until acknowledged, no change in date of timely payment is recognized by NetLojix. The maximum payment required for restoration of service that existed prior to disconnection shall be the total past-due amount, applicable charges and Advance Payment and Deposit as specified elsewhere in this tariff. The Customer is held responsible for all charges for services furnished at the Customer's request and for all toll service furnished. It is the Customer's responsibility to contact NetLojix when no bill is received. Except as provided elsewhere in this tariff, the rate for a full billing period is specified in this tariff. If the prorating indicates a refund is due, the refund is applied as a bill credit.

The Customer is liable for any legal fees incurred by NetLojix in the process of collecting a past-due amount. The amount of these fees can be determined by officers of court if the proceedings are fully litigated. If the Customer acquiesces to NetLojix's demand for payment before a judgment is rendered, NetLojix will bill the delinquent customer for costs incurred to that point. The Customer is entitled to a statement of legal fees that are being assessed.

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SECTION 2 - REGULATIONS (Cont'd)**2.6 Rendering and Payment of Bills (Cont'd)****2.6.4 Disputed Bills**

In the event of a dispute concerning a bill, NetLojix may require the Customer to pay the undisputed portion of the bill. Following payment of the undisputed amount, efforts to resolve the complaint, using complaint procedures in this tariff, shall continue for no more than forty-five (45) days after the rendering of the disputed bill. During this period the service shall not be disconnected for nonpayment of the disputed amount. If there is still a disagreement about the disputed amount after the forty-five (45) days period, the Customer may file an appropriate complaint with the South Dakota Public Utilities Commission at the address referenced in section 2.6.5 of this tariff. The Customer will not be required to pay the disputed portion of the bill while the complaint is pending before the Commission.

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SECTION 2 – REGULATIONS (Cont'd)

2.6 Rendering and Payment of Bills (Cont'd)

2.6.5 Customer Complaints

Customer complaints are handled by a full service customer service department. A customer or prospective customer may initiate a complaint or billing inquiry with NetLojix by either calling 1-877-NETLOJIX during normal business hours or submitting a written complaint to:

NetLojix Telecom, Inc.
501 Bath Street
Santa Barbara, CA 93101

NetLojix's response to the customer will generally be in the same form used by the customer. However, NetLojix may respond to written complaints by telephone when it believes such communications will be more effective in resolution of the issue. When a complaint or billing inquiry is received, a NetLojix customer service representative will determine if the call was processed by NetLojix, and if so, the type of call. If it is a fraud or unanswered call for which the customer should not be held responsible, NetLojix will refund all charges for the call. If there is a rate dispute, NetLojix will adjust the charges if an error is confirmed. The customer may at any point during the resolution of the complaint or billing inquiry seek review by a NetLojix supervisor or manager. If the customer wishes further review after investigation and final resolution by NetLojix, the customer may direct all appropriate information to the Federal Communications Commission or the South Dakota Public Utilities Commission, located at 500 E. Capitol Avenue, State Capitol Building, Pierre, SD 57501, telephone number (605) 773-3201 or 1-800-332-1782 or TTY Through Relay South Dakota at 1-800-877-1113.

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SECTION 2 – REGULATIONS (Cont'd)**2.6 Rendering and Payment of Bills (Cont'd)****2.6.6 Discontinuance of Service**

Company may terminate Service to a Customer for nonpayment of undisputed charges or other violation of this tariff or provision of law upon written notice, as required below, to the Customer without incurring any liability for damages due to loss of telephone Service to the Customer. Termination of Service will not occur on any Friday, Saturday, Sunday or legal holidays. Charges will not be considered past due until thirty (30) days from the closing date printed on the Customer's bill.

The Company may refuse or discontinue Service under the following conditions provided that the Customer shall be given five (5) days written notice, excluding Sundays and legal holidays, to comply with any rule or remedy any deficiency:

- A. For non-compliance with or violation of any State, municipal, or Federal law, ordinance or regulation pertaining to telephone Service, including, but not limited to, the placement of harassing, annoying or repeated unwanted calls of which the Company receives notice.
- B. For use of telephone Service for any purpose other than that described in the application.
- C. For neglect or refusal to provide reasonable access to the Company or its agents for the purpose of inspection and maintenance of equipment owned by the Company or its agents.
- D. For noncompliance with or violation of Commission regulation or the Company's rules and regulations on file with the Commission.

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SECTION 2 – REGULATIONS (Cont'd)

2.6 Rendering and Payment of Bills (Cont'd)

2.6.6 Discontinuance of Service (Cont'd)

- E. For failure of Customer to pay a bill for utility service when due.
- F. For failure of Customer to meet the Company's credit requirements.
- G. Without notice in the event of Customer use of equipment or services in such a manner as to adversely affect the Company's equipment or Service to others.
- H. Without notice in the event of tampering with the equipment or services owned by the Company, the Underlying Company or their agents.
- I. Without notice in the event of a condition determined to be hazardous to the Customer, to other Customers of the Company, to the Company's equipment, the public, or to employees of the Company.

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SECTION 2 – REGULATIONS (Cont'd)**2.7 Taxes And Fees**

Now, or at any future time, if a state or municipality possesses or acquires the legal right to impose an occupation tax, license tax, sales tax, gross receipts tax, permit fee, franchise fee or other similar charge upon NetLojix, and has imposed, or imposes the same by ordinance or otherwise, such taxes, fees or charges shall be billed to the customers receiving service within the territorial limits of such municipality. Such billing shall allocate the tax, fee or charge among customers uniformly on the basis of each customer's monthly charges for the types of service made subject to such tax, fee or charge.

If at any future time a county or other local taxing authority acquires the legal right to impose an occupation tax, license tax, sales tax, gross receipts tax, permit fee, franchise fee or other similar charge upon NetLojix, and has imposed, or imposes the same by ordinance or otherwise, such taxes, fees or charges shall be billed to the customers receiving service within the territorial limits of such municipality. Such billing shall allocate the tax, fee or charge among customers uniformly on the basis of each customer's monthly charges for the types of service made to such tax, fee or charge.

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SECTION 3 – EXPLANATION OF RATES**3.1 Timing of Calls**

The Customer's long distance usage charge is based on the actual usage of NetLojix's network. Usage begins when the called party picks up the receiver. When the called party picks up, is determined by hardware answer supervision in which the local telephone company sends a signal to the switch or the software utilizing audio tone detection. A call is terminated when either calling party hangs up.

3.2 Uncompleted Call Crediting

If A Customer receives a bill for an uncompleted call, NetLojix will reimburse the customer for the full amount.

3.3 Minimum Call Completion Rate

A Customer can expect a call completion rate (number of calls completed/number of calls attempted) of not less than 95% during peak use periods for all FGD services.

3.4 Rates Based Upon Calculation of Distance

Usage charges for all mileage sensitive products are based on the airline distance between rate centers associated with the originating and terminating points of the call.

The airline mileage between rate centers is determined by applying the formula below to the vertical and horizontal coordinates associated with the rate centers involved. The Company uses the rate centers that are produced by Bell Communications Research in the NPA-NXX V & H Coordinates Tape and Bell's NECA Tariff No. 4.

FORMULA: The square
 root of: $\frac{(V1 - V2)^2 + (H1 - H2)^2}{10}$

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SECTION 4 – SERVICE OFFERINGS

4.1 Long Distance Service

Company's Long Distance Service (LDS) is a communications service which is available for use by customers twenty-four (24) hours a day. Customers may originate LDS from locations served by the Carrier, and may terminate in all locations within the State of South Dakota.

The service is offered in Feature Group D (FGD) exchanges where the Customer's local telephone lines are presubscribed by the local exchange company to the Company's LDS service, such that "1+" interLATA calls are automatically routed to the Company's network.

4.2 Toll Free Service

Toll Free Service is an inbound communications service which permits calls to be completed at the Customer's location without charge to the calling party. Access to the service is gained by dialing a ten (10) digit telephone number (800+ NXX-XXXX) which will terminate at the Customer's location. Calls may originate from any location within the State of South Dakota and may terminate at the Customer's location.

Toll Free Service will be billed per call based on the duration of the call. Usage discounts apply to aggregate monthly interstate and intrastate usage.

Toll Free service calls are originated via normal shared use facilities and are terminated via the Customer's local exchange service access line.

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SECTION 4 – SERVICE OFFERINGS (Cont'd)

4.3 Miscellaneous Services

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SECTION 5 – RATES

5.1 Long Distance Service

Rate Per Minute

24 hours a day, 7 days a week,
365 days a year

\$.30

5.2 Toll Free Service

Rate Per Minute

24 hours a day, 7 days a week,
365 days a year

\$.30

5.3 Miscellaneous Services

RESERVED FOR FUTURE USE

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SECTION 5 – RATES

5.4 Late Payment Charge

Interest charges of 1.5% per month will be assessed on all unpaid balances more than thirty days old.

5.5 Return Check Charge

A return check charge of \$25.00 will be assessed for checks returned for insufficient funds.

5.6 Restoration of Service

A restoration fee of \$25.00 per occurrence is charged when service is re-established for customers who had been disconnected for non-payment.

5.7 Directory Assistance Charge

Company will connect LDS Service Customers to Directory Assistance (DA) for a fee of \$0.75 per occurrence.

5.8 Special Promotions

The Company will, from time to time, offer special promotions to its customers waiving certain charges. These promotions will be approved by the Commission with specific starting and ending dates.

5.9 Payphone Surcharge

A charge will apply to calls that originate from any payphone used to access Company's services.

Rate per Call: \$0.24

Issued: November 23, 1999

Effective:

Issued by:

Michael D. Ussery
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

SECTION 5 – RATES

5.10 Special Rates For The Handicapped

5.10.1 Directory Assistance

There shall be no charge for up to fifty (50) calls per billing cycle from lines or trunks serving individuals with disabilities. Company shall charge the prevailing tariff rates for every call in excess of fifty (50) calls within a billing cycle.

5.10.2 Hearing and Speech Impaired Persons

Intrastate toll message rates for TDD users shall be evening rates for daytime calls and night rates for evening and night calls.

5.10.3 Telecommunications Relay Service

The charge for intrastate toll calls received from the relay service, will be 50% percent off of the otherwise applicable rate for a voice nonrelay call except that where either the calling or called party indicates that either party is both hearing and visually impaired, the call shall be discounted 60 percent off of the otherwise applicable rate for a voice nonrelay call. The above discounts apply only to time-sensitive elements of a charge for the call and shall not apply to per call charges such as a credit card surcharge.

307868.2

Issued: November 23, 1999

Effective:

Issued by:

Michael D. Ussery
NetLojix Telecom, Inc.
8721 Airport Freeway
Fort Worth, TX 76180

**BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF SOUTH DAKOTA**

**IN THE MATTER OF THE APPLICATION OF)
NETLOJIX TELECOM, INC. FOR A)
CERTIFICATE OF AUTHORITY TO PROVIDE)
TELECOMMUNICATIONS SERVICES IN)
SOUTH DAKOTA)**

**ORDER GRANTING
CERTIFICATE OF
AUTHORITY**

TC99-108

On November 23, 1999, the Public Utilities Commission (Commission), in accordance with SDCL 49-31-3 and ARSD 20:10:24:02, received an application for a certificate of authority from NetLojix Telecom, Inc. (NetLojix).

NetLojix proposes to provide resold intrastate interexchange telecommunications services. These services will include direct dialed 1+ service, inbound/outbound message telecommunications service, switched and dedicated services, toll free and post-paid calling service to and from all points within South Dakota. A proposed tariff was filed by NetLojix. The Commission has classified long distance service as fully competitive.

On November 24, 1999, the Commission electronically transmitted notice of the filing and the intervention deadline of December 10, 1999, to interested individuals and entities. No petitions to intervene or comments were filed and at its December 28, 1999, meeting, the Commission considered NetLojix's request for a certificate of authority. Commission Staff recommended granting a certificate of authority, subject to the condition that NetLojix not offer a prepaid calling card or require deposits or advance payments without prior approval of the Commission. Commission Staff further recommended a waiver of ARSD 20:10:24:02(8).

The Commission finds that it has jurisdiction over this matter pursuant to SDCL Chapter 49-31, specifically 49-31-3 and ARSD 20:10:24:02 and 20:10:24:03. The Commission finds that NetLojix has met the legal requirements established for the granting of a certificate of authority. NetLojix has, in accordance with SDCL 49-31-3, demonstrated sufficient technical, financial and managerial capabilities to offer telecommunications services in South Dakota. Further, the Commission finds that there is good cause to waive ARSD 20:10:24:02(8). The Commission approves NetLojix's application for a certificate of authority, subject to the condition that NetLojix not offer a prepaid calling card or require deposits or advance payments without prior approval of the Commission. As the Commission's final decision in this matter, it is therefore

ORDERED, that NetLojix's application for a certificate of authority is hereby granted, effective January 23, 2000, subject to the condition that NetLojix not offer a prepaid calling card or require deposits or advance payments without prior approval of the Commission. It is

FURTHER ORDERED, that the Commission finds good cause to waive ARSD 20:10:24:02(8). It is

FURTHER ORDERED, that NetLojix shall file informational copies of tariff changes with the Commission as the changes occur.

Dated at Pierre, South Dakota, this 12th day of January, 2000.

CERTIFICATE OF SERVICE The undersigned hereby certifies that this document has been served today upon all parties of record in this docket, as listed on the docket service list, by first class mail, in properly addressed envelopes, with charges prepaid thereon. By: <u>Melaine Kalbo</u> Date: <u>1/13/00</u> (OFFICIAL SEAL)

BY ORDER OF THE COMMISSION:

James A. Burg
JAMES A. BURG, Chairman

Pam Nelson
PAM NELSON, Commissioner

Laska Schoenfelder
LASKA SCHOENFELDER, Commissioner

SOUTH DAKOTA PUBLIC UTILITIES COMMISSION

CERTIFICATE OF AUTHORITY

**To Conduct Business As A Telecommunications Company
Within The State Of South Dakota**

Authority was Granted December 28, 1999, effective January 23, 2000
Docket No. TC99-108

This is to certify that

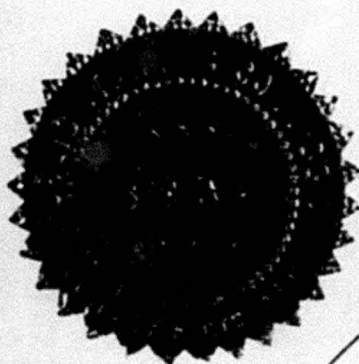
NETLOJIX TELECOM, INC.

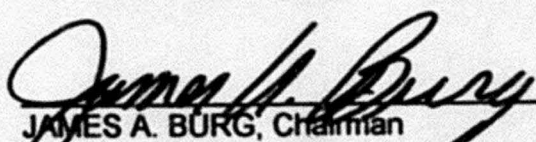
is authorized to provide telecommunications services in South Dakota.

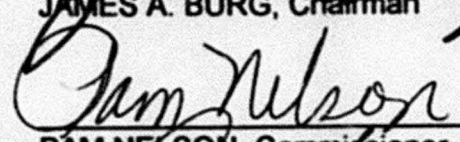
This certificate is issued in accordance with SDCL 49-31-3 and ARSD 20:10:24:02, and is subject to all of the conditions and limitations contained in the rules and statutes governing its conduct of offering telecommunications services.

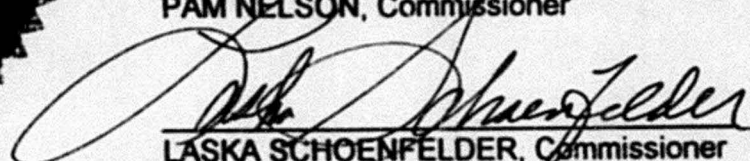
Dated at Pierre, South Dakota, this 12th day of January, 2000.

**SOUTH DAKOTA PUBLIC
UTILITIES COMMISSION:**




JAMES A. BURG, Chairman


PAM NELSON, Commissioner


LASKA SCHOENFELDER, Commissioner