SUNAIR SERVICES CORP
Form DEF 14A
January 26, 2006

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
SCHEDULE 14A
(RULE 14a-101)
INFORMATION REQUIRED IN PROXY STATEMENT
SCHEDULE 14A INFORMATION
Proxy Statement Pursuant to Section 14(A)
of the Securities Exchange Act of 1934

Filed by the registrant þ
Filed by a party other than the registrant o
Check the appropriate box:
o Preliminary proxy statement
o **Confidential, For Use of the Commission only (as permitted by Rule 14a-6(e)(2))**
þ Definitive proxy statement
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SUNAIR SERVICES CORPORATION

(Name of Registrant as Specified in Its Charter)

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SUNAIR SERVICES CORPORATION
3005 S.W. THIRD AVENUE
FT. LAUDERDALE, FL 33315
NOTICE OF ANNUAL MEETING OF SHAREHOLDERS
TO BE HELD ON FEBRUARY 13, 2006

To our shareholders:

The Annual Meeting of Shareholders (the Annual Meeting) of Sunair Services Corporation (the Company, us, our or we) will be held on February 13, 2006, at 11:00 a.m., local time, at the Hilton Hotel, 100 Fairway Drive, Deerfield Beach, Florida, 33441, for the following purposes:

(1) To elect six members to our Board of Directors, each to serve until the next Annual Meeting of Shareholders or until their successors have been duly elected and qualified;

(2) To consider and act upon a proposal to amend and restate our Articles of Incorporation to incorporate all previously approved amendments to our Articles of Incorporation, to delete information that is solely of historical interest, to conform our Articles of Incorporation to our bylaws, including an indemnification provision, and to make other minor stylistic, definitional and clarifying drafting alterations; and

(3) To act upon such other business as may properly come before the Annual Meeting and any and all adjournments or postponements of the Annual Meeting.

All shareholders of record at the close of business on January 24, 2006 will be entitled to vote at the Annual Meeting or any adjournments or postponements thereof.

By Order of the Board of Directors

/s/ SYNNOTT B. DURHAM

Synnott B. Durham
Secretary and Chief Financial Officer

Fort Lauderdale, FL
January 26, 2006

This is an important meeting and you are invited to attend the Annual Meeting in person. Whether or not you expect to be present at the Annual Meeting, please complete, sign and date the enclosed proxy card and return it promptly in the enclosed return envelope. No postage is required if mailed in the United States. Shareholders who execute a proxy card may nevertheless attend the Annual Meeting, revoke their proxy and vote their shares in person.

SUNAIR SERVICES CORPORATION
3005 S.W. THIRD AVENUE
FT. LAUDERDALE, FL 33315

PROXY STATEMENT
ANNUAL MEETING OF SHAREHOLDERS

This proxy statement is furnished in connection with the solicitation by the Board of Directors of Sunair Services Corporation (the Company, us, our or we), of proxies to be used with respect to the matters to be voted upon at the Annual Meeting of Shareholders (the Annual Meeting) to be held on February 13, 2006, at 11:00 a.m., local time, at the Hilton Hotel, 100 Fairway Drive, Deerfield Beach, Florida, 33441, and at any adjournments or postponements thereof.

The approximate date that this proxy statement and the enclosed form of proxy are first being sent to shareholders is January 26, 2006. You should review the information provided in this proxy statement together with our Annual Report on Form 10-KSB for the fiscal year ended September 30, 2005, which is being delivered to shareholders simultaneously with this proxy statement. The cost of solicitation of proxies is being borne by the Company.

PURPOSES OF THE ANNUAL MEETING

At the Annual Meeting, our shareholders will consider and vote upon the following matters:

(1) the election of six members to our Board of Directors, each to serve until the next Annual Meeting of Shareholders or until their successors have been duly elected and qualified;

(2) a proposal to amend and restate our Articles of Incorporation to incorporate all previously approved amendments to our Articles of Incorporation, to delete information that is solely of historical interest, to conform our Articles of Incorporation to our bylaws, including an indemnification provision, and to make other minor stylistic, definitional and clarifying drafting alterations; and

(3) such other business as may properly come before the Annual Meeting and any and all adjournments or postponements of the Annual Meeting.

Our Board of Directors has determined that the: (i) election of the six nominees to our Board of Directors; and (iii) amendment and restatement of our Articles of Incorporation are in our best interests and the best interests of our shareholders. Our Board of Directors has approved the nomination of, and unanimously recommends that you vote to elect, each of the six nominees to our Board of Directors. In addition, our Board of Directors has approved, and unanimously recommends that you vote in favor of the proposal to amend and restate our Articles of Incorporation.

As of the record date, January 24, 2006, 12,186,380 shares of our common stock were issued and outstanding. Only shareholders of record as of the close of business on such date will be entitled to notice of, and to vote at, the Annual Meeting. Proxies may be revoked at any time prior to the Annual Meeting by giving written notice of revocation to our corporate Secretary, by giving a later dated proxy, or by attending the Annual Meeting and voting in person.

Brokers who hold shares in street name for customers have the authority under the rules of the various stock exchanges to vote on certain items when they have not received instructions from the beneficial owners of our common stock. Brokers that do not receive instructions from such beneficial owners of our common stock are entitled to vote those shares with respect to Proposals 1 and 2. Shares for which brokers have not received instructions, and therefore are not voted with respect to a certain proposal, are referred to as broker non-votes.

Under Florida law and our Articles of Incorporation, the presence in person or by proxy of shareholders entitled to cast a majority of all votes entitled to be cast on the matters at the Annual Meeting constitutes a quorum. A share that is represented for any purpose is deemed present for quorum purposes. Therefore, abstentions and broker non-votes will count for purposes of determining if there is a quorum present at the Annual Meeting, will have no effect on Proposal 1 and will count as no votes for the other Proposals.

This proxy statement is first being mailed to our shareholders on or about January 26, 2006. A copy of our Annual Report on Form 10-KSB for the fiscal year ended September 30, 2005, except for exhibits, accompanies this proxy statement and is incorporated in this proxy statement by reference. Upon request, we will provide copies of the exhibits to the Annual Report on Form 10-KSB at no additional cost. All requests for copies should be directed to our corporate Secretary c/o Sunair Services Corporation, 3005 S.W. Third Avenue, Ft. Lauderdale, FL 33315.

TABLE OF CONTENTS

ANNEXES:

VOTING SECURITIES

Date; Time; Venue

Our Annual Meeting of Shareholders (the Annual Meeting) will be held on February 13, 2006, at 11:00 a.m., local time, at the Hilton Hotel, 100 Fairway Drive, Deerfield Beach, Florida, 33441.

Quorum

The presence, in person or by proxy, of the holders of shares representing a majority of the outstanding shares of our common stock will constitute a quorum.

Shareholder Vote Necessary to Approve Proposals

The affirmative vote of a plurality of the votes cast by our shareholders is required to approve the election of the six nominees to our Board of Directors, as described in Proposal 1.

The affirmative vote of the holders of a majority of the shares of our common stock entitled to vote on the matter is required to approve the proposal to amend and restate our Articles of Incorporation, as described in Proposal 2.

If any other matters should properly come before the Annual Meeting, proxies will be voted on these other matters in accordance with the judgment of the persons voting the proxies.

Proxy and Voting Mechanics

If you hold shares of our common stock at the close of business on January 24, 2006, the record date, you are entitled to vote at the Annual Meeting. Each share of our common stock is entitled to one vote upon all matters to be acted upon at the Annual Meeting. As of the record date, there were 12,186,380 shares of our common stock issued and outstanding.

Abstentions are considered as shares present and entitled to vote for purposes of determining the outcome of any matter submitted to the shareholders for a vote, but are not counted as votes cast for or against any matter. The inspector of elections will treat shares referred to as broker or nominee non-votes (shares held by brokers or nominees as to which instructions have not been received from the beneficial owners or persons entitled to vote and the broker or nominee does not have discretionary voting power on a particular matter) as shares that are present and entitled to vote for purposes of determining the presence of a quorum. For purposes of determining the outcome on proposals as to which the proxies reflect broker or nominee non-votes, shares represented by these proxies will be treated as not present and not entitled to vote on that subject matter. Accordingly, these shares would not be considered by the inspectors as shares entitled to vote on that subject matter and therefore would not be considered by the inspector when counting votes cast on the matter.

Your vote is important. Accordingly, you are urged to sign, date and return the accompanying proxy card whether or not you plan to attend the Annual Meeting. If you do attend, you may vote by ballot at the Annual Meeting, which will have the effect of canceling any proxy previously given.

If the enclosed proxy is properly signed, dated and returned, the shares represented by the proxy will be voted in accordance with the instructions on the proxy card. If no instructions are indicated, the shares represented by the proxy will be voted in the following manner:

(i) FOR the election of each of the nominees for director; and

(ii) FOR the proposal to amend and restate our Articles of Incorporation.

If any other matters should properly come before the Annual Meeting, proxies will be voted on these other matters in accordance with the judgment of the persons voting the proxies. Discretionary authority to vote on such matters is conferred only by the granting of these proxies.

Any shareholder giving a proxy may revoke it by written notice to our corporate Secretary at the address provided above at any time before it is exercised. Attendance at the Annual Meeting will not have the effect of revoking the proxy unless this written notice is given or unless the shareholder votes by ballot at the Annual Meeting.

Costs of Proxy Solicitation

We will bear the cost of preparing, printing, assembling and mailing all proxy materials that may be sent to shareholders in connection with this solicitation. Arrangements will also be made with brokerage houses, other custodians, nominees and fiduciaries, to forward soliciting material to the beneficial owners of shares of our common stock held by these persons. We will reimburse these persons for reasonable out-of-pocket expenses incurred by them. In addition to the solicitation of proxies by use of the mails, our officers and regular employees may solicit proxies without additional compensation by telephone or telegraph. We do not expect to pay any compensation for the solicitation of proxies.

PROPOSAL NO. 1

Election of Directors

Our directors are elected annually at the Annual Meeting of Shareholders and hold office until their death, resignation, retirement, removal, disqualification, or the next Annual Meeting of Shareholders or until their successors are duly elected and qualified.

The number of directors constituting the full Board of Directors currently is seven, and the term of each director will expire at the Annual Meeting. As disclosed previously, Michael D. Herman, a current director, has elected not to stand for re-election at the Annual Meeting. Mr. Herman has not expressed any disagreement with us involving any aspect of our operations, internal controls, policies or practices and we are not aware of any such basis for Mr. Herman s decision not to stand for re-election.

As a result of Mr. Herman s decision not to stand for re-election to the Board of Directors, only six directors will be elected at the Annual Meeting. The remaining board seat will remain vacant until the Board of Directors has identified a suitable candidate. The vacancy will be filled by the affirmative vote of a majority of the Board of Directors, in accordance with our bylaws.

Except for Mr. Herman, all of the directors whose regular terms of office expire at the upcoming Annual Meeting have been nominated for re-election to our Board of Directors at the Annual Meeting. Information about each of the nominees is given below. If elected, each of the nominees shall serve until the next Annual Meeting of Shareholders, expected to be held in February 2007, or until their successors have been duly elected and qualified.

We have no reason to believe that any of the nominees will be unable to serve as director. However, in the event that any nominee should become unable or unwilling to serve as a director, the proxy will be voted for the election of the person or persons as shall be nominated by our Board of Directors.

Nominees for Re-election

Joseph S. DiMartino, 61, was appointed to our Board of Directors on September 9, 2005, to fill a vacancy created by James E. Laurent s resignation from our Board of Directors. Mr. DiMartino was nominated by Coconut Palm Capital Investors II, Ltd. (Coconut Palm), in accordance with a previously disclosed Purchase Agreement, dated November 17, 2004, between us and Coconut Palm. Since 1995, Mr. DiMartino has been the Chairman of the Board and a Director of The Dreyfus Family of Mutual Funds in New York City. Mr. DiMartino served as President, Chief Operating Officer and Director of The Dreyfus Corporation from October 1982 until December 1994. Mr. DiMartino also has served since 1997 as a Director and Chairman of the compensation committee of Century Business Services, Inc., and also serves as a Director of Levcor International, Inc. (formerly Carlyle Industries, Inc.), The Newark Group and the Muscular Dystrophy Association. Mr. DiMartino is a 1965 graduate of Manhattan College and attended New York University s Graduate School of Business.

Mario B. Ferrari, 28, was appointed Vice Chairman of our Board of Directors on February 4, 2005, at the Annual Meeting of Shareholders. Mr. Ferrari has served as Principal and Co-Founder of Royal Palm Capital Partners, LLLP, a private investment and management firm, since July 2002. He has also served as a Director of Devcon International Corp, a publicly-held company that provides electronic security and construction services, since July 2004, and as a Director of Coconut Palm Acquisition Corp., a publicly held special purpose acquisition company, since September 2005. Previously, he worked as an investment banker with Morgan Stanley & Co. from 2000 to 2002. Prior to that, from 1997 to 1999, Mr. Ferrari was co-founder of PowerUSA, LLC, a retail energy services company. Mr. Ferrari received his B.S. in Finance and International Business, magna cum laude, from Georgetown University.

Arnold Heggestad, Ph.D., 62, was appointed to our Board of Directors in March 2003. Dr. Heggestad is the Holloway Professor of Finance and Entrepreneurship at the University of Florida and has been at the University since 1974. Dr. Heggestad has served as Chairman, Department of Finance, Insurance and Real Estate, Associate Dean, College of Business Administration, Director of the Center for Financial Institutions, Executive Director, University of Florida Research Foundation, Associate Vice-President of Entrepreneurial Programs in the Office of Research. Dr. Heggestad is a Director of Intrepid Capital Management, Inc. He has been very active in public service and has served both public and private interests in a number of capacities.

Steven P. Oppenheim, 59, was appointed to our Board of Directors in January 2004. Mr. Oppenheim is the President and owner of Oppenheim & Associates, Miami, FL, which, since 2002 has provided a wide range of consulting and strategic planning services to a diversified international clientele in the U.S., Europe and Latin America. Mr. Oppenheim holds a Juris Doctor Degree and maintained his own law firm from 1975 until 2001. From 1973 to 1975 he was tax supervisor for Coopers & Lybrand, CPA s. Mr. Oppenheim serves in various officer capacities for several multinational companies or affiliates involving U.S business. He serves as a Director of the International Advertising Association and as a Director and Chairman of the British American Chamber of Commerce. He previously served as a Director of the French-American Chamber of Commerce, Italy-America Chamber of Commerce, and European-American Chamber of Commerce.

Richard C. Rochon, 48, was appointed Chairman of our Board of Directors on February 4, 2005, at the Annual Meeting of Shareholders. Mr. Rochon has served as Chairman and Chief Executive Officer of Royal Palm Capital Partners LLLP, a private investment and management firm, since 2002. Mr. Rochon also has served as a Director of Devcon International Corp, a publicly-held company that provides electronic security and construction services, since July 2004, and as Chairman and Chief Executive Officer of Coconut Palm Acquisition Company, a publicly held special purpose acquisition company, since September 2005. Previously, from 1987 to 2002, Mr. Rochon served as President of Huizenga Holdings, Inc, a management and holding company owned by H. Wayne Huizenga, whose investments included Blockbuster Entertainment Corporation, Republic Waste Industries, Inc., AutoNation, Inc., and Boca Resorts, Inc. Mr. Rochon joined Huizenga Holdings in 1985 as Treasurer and was promoted to President in 1987. Mr. Rochon served as Vice Chairman of Huizenga Holdings and as sole Director for many of Huizenga Holdings private and public portfolio companies, including as a Director of AutoNation, Inc., the NHL s Florida Panthers and the NFL s Miami Dolphins. Mr. Rochon previously served as Vice Chairman of Boca Resorts, Inc, an owner and operator of luxury resort properties in Florida, from November 1996 to December 2004, while serving as President from March 1998 until January 2002. In addition, Mr. Rochon has been a Director of Bancshares of Florida, a full-service commercial bank, since 2002, and a Director of Century Business Services, a diversified services company, since 1996. From 1979 until 1985 Mr. Rochon was employed as a certified public accountant by the public accounting firm of Coopers & Lybrand. L.L.P. Mr. Rochon received his B.S. in Accounting from Binghamton University (formerly State University of New York at Binghamton) in 1979 and his Certified Public Accounting designation in 1981.

Charles P. Steinmetz, 66, was appointed to our Board of Directors in June 2005. Mr. Steinmetz was nominated by Coconut Palm, in accordance with a previously disclosed Purchase Agreement, dated November 17, 2004, between us and Coconut Palm, and pursuant to a previously disclosed Stock Purchase Agreement, dated June 7, 2005, between our subsidiary, Sunair Southeast Pest Holdings, Inc. (Sunair Pest Holdings), and the selling shareholders of Middleton Pest Control, Inc (Middleton). Mr. Steinmetz was the majority owner of Middleton from 1977 until it was purchased by Sunair Pest Holdings. Mr. Steinmetz also served in various capacities with Orkin Exterminating Company (1961-1973) and Truly Nolen, Inc. (1974-1977), and led the build-up and sale of All America Termite and Pest Control, Inc. (1982-1997), which at the time of sale was the largest privately owned pest control company in the United States with 125 locations throughout Florida, Georgia, Alabama, North and South Carolina, Louisiana, Tennessee, Mississippi, Arizona and Texas. Mr. Steinmetz received his B.S. in Agriculture, major in Entomology, from the University of Florida.

Information Regarding our Board of Directors and Committees of our Board of Directors

Attendance at Board of Directors and Committees Meetings

During the fiscal year ended September 30, 2005, our Board of Directors held 10 meetings and the Audit Committee held 5 meetings. Attendance was 100% at of our Board of Directors meetings and 100% at the Audit Committee meetings.

Directors Fees

Directors who are not full-time employees of our company were paid an annual retainer in fiscal 2005 in the amount of $20,000 and an attendance fee of $1,000 for each meeting of our Board of Directors, plus travel expenses incurred in connection therewith. Beginning in fiscal 2006, directors who are not full-time employees of our company will receive an annual retainer in the amount of $28,000 and an attendance fee of $1,500 for each meeting of our Board of Directors, plus travel expenses incurred in connection therewith. Further, each of the directors who are not full-time employees of our company will receive 5,000 options to purchase shares of our common stock for each year of service, which will vest quarterly during each year of service, and any new directors who are not full-time employees of our company will receive 20,000 options to purchase shares of our common stock upon joining the Board of Directors, which will vest quarterly over the first year of service.

The Audit Committee consists of two Independent Board Members, who were paid $1,000 each for each committee meeting during fiscal 2005. Beginning in fiscal 2006, the Audit Committee chairman will receive an annual retainer in the amount of $5,000 and an attendance fee of $1,500 for each meeting of the Audit Committee, and any other members of the Audit Committee will be paid $1,250 each for each committee meeting.

Directors who are full-time employees of our company are not paid any fees or additional remuneration for services as members of our Board of Directors or any committee thereof.

In consideration of Mr. Herman s efforts on behalf of our company in connection with the equity investment by Coconut Palm, as described under the caption Change in Control beginning on page 12, the Board of Directors unanimously voted to award to Mr. Herman a bonus in the amount of $75,000, payable upon the closing of the Coconut Palm transaction.

Committees and Meetings of our Board

Our Audit Committee is the sole functioning committee of our Board of Directors. For more information about our Audit Committee and its Audit Committee Report, see Audit Committee beginning on page 17.

We do not have a nominating or similar committee. The Independent Board Members perform the functions of a nominating committee including reviewing and recommending to the Board of Directors candidates for directors. Our Board of Directors has not adopted a written charter for the Independent Board Members performing the functions of a nominating committee. If a shareholder wishes to recommend a nominee for director, written notice should be sent to the Corporate Secretary in accordance with the instructions set forth later in this proxy statement under the caption Information Concerning Shareholder Proposals beginning on page 21. Each written notice must set forth: (1) the name and address of the shareholder who is making the nomination; (2) the number of shares of our common stock which are beneficially owned by the shareholder and a representation that the shareholder is a holder of record of our common stock entitled to vote at the annual meeting of shareholders and intends to appear in person or by proxy at the meeting and nominate the person specified in the notice; (3) the name of the director candidate; (4) a complete resume or statement of the candidate s qualifications (including education, work experience, knowledge of our industry, membership on the board of directors of another corporation and civic activity); (5) a description of all arrangements or understandings between the shareholder and the candidate and/or any other person or persons pursuant to which the nomination is to be made by the shareholder; (6) such other information regarding a candidate as would be required to be included in a proxy statement, including information with respect to a candidate s independence as defined under the rules and regulations promulgated by the Securities and Exchange Commission and the American Stock Exchange and information regarding the candidate s attributes that the Independent Board Members would need to consider in order to assess whether such candidate would qualify as an audit committee financial expert as defined by the rules and regulations promulgated by the Securities and Exchange Commission; and (7) the candidate s consent to serve as a director of our company if elected.

The Independent Board Members will evaluate the suitability of potential candidates nominated by shareholders in the same manner as other candidates identified to the Independent Board Members. In making its nominations, the Independent Board Members identify candidates who meet the current challenges and needs of the Board of Directors. In making such decisions, the Independent Board Members consider, among other things, an individual s business experience, industry experience, financial background and experiences and whether the individual meets the independence requirements of the American Stock Exchange. The Independent Board Members use multiple sources for identifying and evaluating nominees for directors including referrals from current directors, recommendations by shareholders and input from third party executive search firms.

We do not have a compensation or similar committee. The Independent Board Members perform the functions of a compensation committee including reviewing and recommending to the Board of Directors the compensation of our executive officers, including salaries, bonuses and benefit plans.

The affirmative vote of a plurality of the votes cast by our shareholders is required to approve the election of each of the nominees set forth in this Proposal 1. You may vote in favor of, or you may withhold your vote from, the nominees. Votes that are withheld with respect to this matter will be excluded entirely from the vote and will have no effect, other than for purposes of determining the presence of a quorum.

Our Board of Directors unanimously recommends that you vote FOR the election of each of the nominees set forth in this Proposal 1.

PROPOSAL NO. 2

Amended and Restated Articles of Incorporation

Since our formation in 1956, our Articles of Incorporation have been amended numerous times to, among other things, change our corporate name, change the number of shares of capital stock we are authorized to issue and set forth provisions relating to our business purpose. Our Board of Directors has determined that it is in our best interests and the best interests of our shareholders to amend and restate our Articles of Incorporation to consolidate the various amendments, to delete information that is solely of historical interest, to conform our Articles of Incorporation to our bylaws, including an indemnification provision, and to make other minor stylistic, definitional and clarifying drafting alterations in a single document.

Specifically, the proposed changes to our Articles of Incorporation will delete the following information, which is solely of historical interest:

- the initial amount of capital required to begin our business;
- the names and addresses of our initial officers, directors and shareholders; and
- the description of our corporate seal.

Further, the following provisions, which are included in our bylaws or otherwise prescribed by law, and are therefore not necessary to be included in our Articles of Incorporation, will be deleted:

- the titles of the designated officers of our company;
- the time and place of our Annual Meeting of Shareholders;
- the requirement that the officers of our company be elected on the same day as the Annual Meeting of Shareholders; and
- extraneous powers granted to our Board of Directors.

We also intend to add an article that will enable us to indemnify our directors, officers, employees and agents to the fullest extent permitted by our bylaws and applicable law, and to make other insignificant drafting alterations and correct typographical and grammatical errors.

The proposed Amended and Restated Articles of Incorporation are not intended to change any existing rights of our shareholders.

A copy of the entire text of the proposed Amended and Restated Articles of Incorporation, which sets forth the amendments discussed above is attached as Annex A to this proxy statement. The above description of the amendments to our Articles of Incorporation is a summary only and you should read the proposed Amended and Restated Articles of Incorporation that are attached to this proxy statement in their entirety.

Under Section 607.1002 of the Florida Business Corporation Act, our Board of Directors may adopt one or more enumerated amendments to our Articles of Incorporation without shareholder action (i.e., extending the duration of our corporation, deleting information that is solely of historical interest, changing our corporate name by substituting Inc. for a similar word or abbreviation in the name, etc). Because some of the proposed amendments to our Articles of Incorporation may be out of the purview of Section 607.1002, such amendments must instead be adopted by a two-step process involving, first the recommendation by our Board of Directors and, second, approval by our shareholders, pursuant to Section 607.1003 of the Florida Business Corporation Act. If the amendments to our Articles of Incorporation are approved at the Annual Meeting of Shareholders, they will become effective upon the filing of the Amended and Restated Articles of Incorporation with the Secretary of State of the State of Florida, which is expected to be accomplished as promptly as practicable after such approval is obtained.

The affirmative vote of the holders of a majority of the shares of our common stock entitled to vote on the matter is required to approve this Proposal 2.

Our Board of Directors has determined that it is in our best interests and the best interests of our shareholders to amend and restate our Articles of Incorporation, and unanimously recommends that you vote FOR this Proposal 2.

CURRENT DIRECTORS AND EXECUTIVE OFFICERS

The following table sets forth our current directors and executive officers. Our directors are elected annually and hold office until their death, resignation, retirement, removal, disqualification, or the next Annual Meeting of Shareholders or until their successors are duly elected and qualified. Our executive officers serve at the discretion of our Board of Directors. There is no family relationship between or among any of our directors and executive officers. Our current Board of Directors consists of seven persons.

Name	Age	Position
Gregory A. Clendenin	52	CEO of Sunair Southeast Pest Holdings, Inc. and Middleton Pest Control, Inc.
Joseph S. DiMartino	61	Director
Synnott B. Durham	64	Chief Financial Officer
Mario B. Ferrari	28	Vice Chairman of the Board
John J. Hayes	53	President and Chief Executive Officer
Arnold Heggestad, Ph.D.	62	Director
Michael D. Herman	48	Director
James E. Laurent	69	President of Sunair Communications, Inc.
Steven P. Oppenheim	59	Director
Richard C. Rochon	48	Chairman of the Board
Charles P. Steinmetz	66	Director

Below is a summary of the business experience of our executive officers who do not serve on our Board of Directors. The business experience of the nominees to our Board of Directors appears under the caption Nominees for Re-election beginning on page 3.

Gregory A. Clendenin, 52, has served as Chief Executive Officer of our wholly-owned subsidiary Sunair Pest Holdings and its wholly-owned subsidiary Middleton, since June 7, 2005, when Middleton was acquired by Sunair Pest Holdings pursuant to a previously disclosed Stock Purchase Agreement, dated June 7, 2005. Previously, Mr. Clendenin served as President and Chief Executive Officer of Middleton since 1996. Mr. Clendenin received his MBA from the Crummer Graduate School of Business at Rollins College.

Synnott B. Durham, 64, has served as our Corporate Secretary since 2003, our Chief Financial Officer since 1994, Vice-President of Finance of our wholly-owned subsidiary Sunair Communications, Inc. since February 2005, and has held various other executive roles with our company since 1979. Mr. Durham received his B.B.A in Accounting from Florida International University.

John J. Hayes, 53, has served as our President and Chief Executive Officer since February 2005. Mr. Hayes previously served as Executive Vice President (2000-2004), President (1987-1989) and Chief Operational Officer (1985-1987) of The TruGreen Companies, and held various other executive roles with The TruGreen Companies since 1975. From 1990-1999, Mr. Hayes served in various capacities as a private investor. Mr. Hayes received his J.D. from the University of Detroit and his B.S. from Michigan State University.

James E. Laurent, 69, has served as President of our wholly-owned subsidiary Sunair Communications, Inc. since February 2005. Mr. Laurent previously served as our President from October 2000 to February 2005, our Chief Executive Officer from December 2000 to February 2005 and as our Vice-President of Marketing beginning in 1988. Mr. Laurent also served on our Board of Directors from December 2000 to September 2005. After retirement from the United States Air Force in 1978, Mr. Laurent held management positions for sales and marketing in the communications-electronics field for international and U.S. government and military market segments.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth, as of the record date (or such other date indicated in the footnotes below), the number and percentage of shares beneficially owned by the following: (i) each person known to us to own beneficially more than 5 percent of the outstanding shares of our common stock; (ii) each of our current directors; (iii) each of our executive officers who had an annual salary and bonus for 2005 in excess of $100,000 and our President and Chief Executive Officer; and (iv) all of our directors and executive officers as a group.

Name[1]	**Number of Shares Beneficially Owned**[2]	**Percent of Common Stock**
Coconut Palm Capital Investors II, Ltd. 595 South Federal Highway Suite 600, Boca Raton, FL 33342 [3]	14,995,900	67.6%
Michael Brauser 595 S. Federal Highway Boca Raton, FL 33432 [4]	1,200,000	9.4%
Trustman c/o STI Classic Small Cap Growth Fund c/o: Trusco Capital Management, Inc. 50 Hurt Plaza, #1400 Atlanta, GA 30303 [5]	1,000,000	8.2%
Joseph S. DiMartino [6]	5,000	*
Mario B. Ferrari [7]	14,997,150	67.6%
Arnold Heggestad, Ph.D. [8]	29,250	*
Michael D. Herman	2,056,700	16.9%
James E. Laurent [9]	57,663	*
Steven P. Oppenheim [10]	21,250	*
Richard C. Rochon [11]	14,997,150	67.6%
Charles P. Steinmetz [12]	412,774	3.4%
Gregory A. Clendenin [13]	205,761	1.7%
Synnott B. Durham [14]	38,658	*
John J. Hayes [15]	623,266	4.9%
All directors and executive officers as a group (11 persons) [16]	18,448,722	80.5%

* Less than 1%.

(1) Except as otherwise indicated, the address of each person named in this table is c/o Sunair Services Corporation, 3005 S.W. Third Avenue, Fort Lauderdale, Florida 33315.

(2) In determining the number and percentage of shares beneficially owned by each person, shares that may be acquired by such person pursuant to options or warrants exercisable within 60 days after the record date are deemed outstanding for purposes of determining the total number of outstanding shares for such person and are not deemed outstanding for such purpose for all other shareholders. To our knowledge, except as otherwise indicated, beneficial ownership includes sole voting and dispositive power with respect to all shares owned by them.

(3) Consists of 4,995,900 shares of our common stock and 10,000,000 shares of our common stock

underlying warrants issued to Coconut Palm that are immediately exercisable. Coconut Palm has the sole power to dispose of 13,370,000 shares of common stock beneficially owned by it. Coconut Palm has the sole power to vote, or to direct the vote of, 14,995,900 shares of Common Stock. 1,625,900 of the 14,995,900 shares of our common stock consist of an aggregate of 810,900 shares of common stock and 815,000 shares underlying warrants that are immediately exercisable, which Coconut Palm has the sole power to vote pursuant to proxy agreements that were executed by certain limited partners of Coconut Palm upon their redemption of their limited partnership interests for shares of our common stock and warrants to purchase shares of our common stock beneficially owned by Coconut Palm. Richard C. Rochon, Chairman of our Board of Directors, and Mario B. Ferrari, Vice Chairman of our Board of Directors, are the natural persons who exercise voting and investment control over the shares.

(4) Mr. Brauser acquired such shares upon the redemption of his limited partnership interests in Coconut Palm and has granted Coconut Palm the sole power

to vote such shares pursuant to a proxy agreement. Includes 600,000 shares underlying warrants that are immediately exercisable.

(5) Includes 300,000 shares of common stock that Trustman has the right (and obligation) to acquire on or about January 27, 2006 pursuant to a Purchase Agreement dated December 15, 2005 between us and Trustman, because satisfaction of the only material condition to such acquisition, the approval of the issuance of such shares by our shareholders, has been obtained. Mark Garfinkel exercises voting and dispositive power over such shares.

(6) Consists of 5,000 shares issuable upon

exercise of options that are exercisable within 60 days after the record date.

(7) Shares consist of: (i) all shares beneficially owned by Coconut Palm. Assumes beneficial ownership of such shares is attributed to Mr. Ferrari. Mr. Ferrari disclaims beneficial ownership of these shares; and (ii) 1,250 shares issuable upon exercise of options directly owned by Mr. Ferrari, which are exercisable within 60 days after the record date.

(8) Includes 21,250 shares issuable upon exercise of options that are exercisable within 60 days after the record date.

(9) Includes 21,658 shares issuable upon exercise of options that are exercisable within 60 days after the record

date.

(10) Consists of 21,250 shares issuable upon exercise of options that are exercisable within 60 days after the record date.

(11) Shares consist of: (i) all shares beneficially owned by Coconut Palm. Assumes beneficial ownership of such shares is attributed to Mr. Rochon. Mr. Rochon disclaims beneficial ownership of these shares; and (ii) 1,250 shares issuable upon exercise of options directly owned by Mr. Rochon, which are exercisable within 60 days after the record date.

(12) Includes 1,250 shares issuable upon exercise of options that are exercisable within 60 days after the record date.

(13) The shares are held by The

Gregory A. Clendenin Trust, of which Mr. Clendenin is the trustee.

(14) Includes 21,658 shares issuable upon exercise of options that are exercisable within 60 days after the record date.

(15) Includes 41,666 shares issuable upon exercise of options that are exercisable within 60 days after the record date. Also includes 290,800 shares of our common stock and 290,800 shares underlying warrants that Mr. Hayes has the immediate right to acquire as a limited partner of Coconut Palm. Upon his acquisition of the shares that Mr. Hayes has the right to acquire as a limited partner of Coconut Palm, Coconut Palm will have the sole power to vote such shares.
Mr. Hayes began serving as

our President and Chief Executive Officer in February, 2005.

(16) Includes 10,717,832 shares issuable upon exercise of options and warrants that are immediately exercisable or are exercisable within 60 days after the record date.

Change in Control

On February 8, 2005, we closed a transaction with Coconut Palm, which we entered into on November 17, 2004. Coconut Palm purchased from us 5,000,000 units (the Units) for an aggregate purchase price of $25 million. Each Unit consisted of (i) one share of our common stock, (ii) one warrant to purchase one share of our common stock at an exercise price of $6.00 per share with a term of three years and (iii) one warrant to purchase one share of our common stock at an exercise price of $7.00 per share with a term of five years. Coconut Palm obtained the $25 million in a private placement of its equity. Following the closing of the transaction, Coconut Palm beneficially owned 15 million shares, or 78.9%, of our then outstanding shares of common stock. Currently, Coconut Palm beneficially owns 67.6% of our outstanding shares of common stock.

Compliance with Section 16(a) of the Securities Exchange Act of 1934

Section 16(a) of the Securities Exchange Act of 1934 requires our directors and executive officers, and persons who own more than 10 percent of our common stock, to file with the Securities and Exchange Commission initial reports of ownership and reports of changes in ownership of our common stock. Officers, directors and greater than 10 percent shareholders are required by the rules and regulations of the Securities and Exchange Commission to furnish us with copies of all Section 16(a) forms they file.

To our knowledge, based solely on review of the copies of these reports furnished to us and representations that no other reports were required, during the fiscal year ended September 30, 2005, all Section 16(a) filing requirements applicable to our officers, directors and greater than 10 percent beneficial owners were complied with, except Mr. Brauser was late in filing his Form 3 and each of Mr. Durham, Mr. Hayes, Mr. Heggestad, Mr. Laheney, Mr. Laurent and Mr. Oppenheim were late in filing one Form 4 for one transaction. In addition, Mr. Budde, who as of June 2005 is no longer an executive officer of our company, was late in filing one Form 4 for one transaction.

EXECUTIVE COMPENSATION

Summary Compensation Table

The following table sets forth compensation awarded to, earned by or paid to: (i) our President and Chief Executive Officer; and (ii) each of our other named executive officers who earned $100,000 or more during Fiscal 2005, 2004 and 2003 (the Named Executive Officers).

		Annual Compensation			Long Term Compensation			
					Awards		Payouts	
Name and Principal Position	**Fiscal Year**	**Salary**	**Bonus**	**Other Annual Compensation**	**Restricted Stock Awards**	**Options/ SARs**	**LTIP Payments**	**All Other Compensation**
John J. Hayes[1] President and Chief Executive Officer	2005	$ 210,625		*		166,667		
Gregory A. Clendenin[2] CEO of Sunair Southeast Pest Holdings, Inc. and Middleton Pest Control, Inc.	2005	$ 110,884		*		47,625		
Synnott B. Durham	2005	$ 124,115				40,000		$ 3,408(3)
Chief Financial Officer	2004	$ 110,000						$ 3,853
	2003	$ 100,000						$ 296
James E. Laurent	2005	$ 147,279				40,000		$ 3,251(4)
President of Sunair	2004	$ 137,500						$ 3,781
Communications, Inc.	2003	$ 125,000						$ 2,222

* Value of perquisites and other personal benefits paid does not exceed the lesser of $50,000 or 10% of the total annual salary and bonus reported for the Named Executive Officer.

(1) Mr. Hayes became our President and CEO effective February 9, 2005.

(2) Mr. Clendenin became the CEO of Sunair Southeast Pest Holdings, Inc. and Middleton Pest Control, Inc. effective June 7, 2005.

(3) Includes $3,146 in company matching contributions to our 401(k) plan and $262 in premiums for term life insurance on the Named Executive Officer.

(4) Includes $3,080 in company matching contributions to our 401(k) plan and $171 in premiums for term life insurance on the Named Executive Officer.

Option Grants

The following table sets forth the individual grants of stock options made by us during the fiscal year ended September 30, 2005 to our Named Executive Officers.

Name	Number of Securities Underlying Options Granted	Percent of Total Options Granted to Employees in Fiscal 2005	Exercise Price	Expiration Date
John J. Hayes	166,667(1)	34.7%	$ 5.00	11/16/2014
Gregory A. Clendenin	47,625(2)	9.9%	$ 11.40	06/07/2013
Synnott B. Durham	40,000(3)	8.3%	$ 13.78	02/08/2013
James E. Laurent	40,000(3)	8.3%	$ 13.78	02/08/2013

(1) These options vest in four equal annual installments beginning on November 16, 2005.

(2) These options vest in four equal annual installments beginning on June 7, 2006.

(3) These options vest at a rate of 1,666 per full month of employment beginning March 8, 2005, except that at the end of two years, all remaining options will vest and become exercisable.

Aggregated Fiscal Year-End Option Value Table

The following table sets forth, with respect to each of our Named Executive Officers, the number of share options exercised and the dollar value realized from those exercises during the 2005 fiscal year and the total number and aggregate dollar value of exercisable and non-exercisable stock options held on September 30, 2005.

Name	Shares Acquired on Exercise (#)	Value Realized ($)	Number of Securities Underlying Unexercised Options at Fiscal Year-End (#)		Value of Unexercised In-the-Money Options at Fiscal Year-End ($)(1)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
John J. Hayes			41,666	124,999	$ 104,165	$ 312,497
Gregory A. Clendenin				47,625		
Synnott B. Durham	29,900	$ 196,967	11,662	28,338		
James E. Laurent	25,000					

Table of Contents

such subsidiary guarantor s existing and future subordinated indebtedness, and will be effectively subordinated in right of payment to all of such subsidiary guarantor s existing and future secured obligations, including its guarantees of PAETEC Holding s existing senior secured credit facilities and the 8 7/8% senior secured notes, to the extent of the value of the collateral securing such obligations.

As of March 31, 2011, following the closing of the offering of the original notes and our use of the net offering proceeds to pay the merger consideration and other costs and expenses related to our acquisition of Cavalier, we had $1,425 million aggregate principal amount of senior indebtedness outstanding, $675 million of which was senior secured indebtedness.

Optional Redemption

We may redeem some or all of the exchange notes, at any time before December 1, 2014, at a redemption price equal to 100% of their principal amount plus a make-whole premium, together with accrued and unpaid interest, if any, to, but excluding the redemption date. We may redeem some or all of the exchange notes, at any time on or after December 1, 2014, at the redemption prices described in this prospectus, together with accrued and unpaid interest, if any, to, but excluding, the redemption date.

Before December 1, 2013, we may redeem up to 35% of the aggregate principal amount of the notes and any additional notes initially issued under the indenture that will govern the exchange notes at a redemption price equal to 109.875% of the principal amount thereof, plus accrued and unpaid interest, if any, to, but excluding, the redemption date, with the net cash proceeds of one or more equity offerings, except that at least 65% of the principal amount of the notes and any such additional notes initially issued must remain outstanding immediately after giving effect to such redemption. For additional information, see Description of the Exchange Notes Optional Redemption.

Mandatory Offers to Purchase

If we experience certain kinds of changes of control, we must offer to repurchase the exchange notes at 101% of their principal amount, plus accrued and unpaid interest. For additional information, see Description of the Exchange Notes Certain Covenants Repurchase of Notes Upon a Change of Control.

If we sell certain of our assets and do not apply the net proceeds to repay indebtedness under our senior secured credit facilities, the 8 $^{7}/8$% senior secured notes or other indebtedness secured on a first-priority basis or to reinvest in our business, we must offer to purchase the exchange notes at 100% of their principal amount, plus accrued and unpaid interest. For additional information, see Description of the Exchange Notes Certain Covenants Limitation on Asset Sales.

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

10

Table of Contents

RISK FACTORS

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

Risks Related to Investing in the Exchange Notes

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

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

14

Table of Contents

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

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

Risks Related to Our Business

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

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

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

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

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

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

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

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

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

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

Table of Contents

operating costs. Federal and state regulations also determine the level of contribution payments PAETEC must make to the federal Universal Service Fund and other federal and state telecommunications subsidy programs, as well as the terms under which it may use any rights-of-way necessary for the operation of its business. If PAETEC fails to comply with applicable regulations, or if the regulations change in a manner adverse to PAETEC, its business and operating results may suffer.

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

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

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

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

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

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

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

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

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

Industry consolidation and realignment may increase PAETEC s costs.

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

Table of Contents

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

The development and expansion of PAETEC s network will require substantial capital investment. If PAETEC chooses to accelerate the expansion of its business, PAETEC will require additional capital. PAETEC also may require additional capital to fund payments of its indebtedness as an increasing amount of such indebtedness becomes due and payable. If PAETEC cannot successfully obtain additional equity or debt financing for necessary purposes on acceptable terms, PAETEC could be at a competitive disadvantage relative to competitors with significant capital or the ability to raise significant capital for expansion. The terms of any financing PAETEC does obtain may be burdensome to PAETEC.

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

Table of Contents

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

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

Table of Contents

FORWARD-LOOKING STATEMENTS

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

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

Table of Contents

USE OF PROCEEDS

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

Table of Contents

RATIO OF EARNINGS TO FIXED CHARGES

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

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

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

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

Table of Contents

SELECTED HISTORICAL CONSOLIDATED FINANCIAL AND OPERATING DATA

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

Table of Contents

UNAUDITED PRO FORMA CONDENSED COMBINED FINANCIAL INFORMATION

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

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

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

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

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

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

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

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

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

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

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

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

Table of Contents

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

Issuance and Sale of 9 7/8% Senior Notes and Acquisition of Cavalier. On December 2, 2010, PAETEC Escrow Corporation, or PAETEC Escrow, a wholly-owned subsidiary of PAETEC Holding Corp., issued and sold $450 million in aggregate principal amount of its 9 7/8% senior notes due 2018. On December 2, 2010, the gross proceeds of approximately $435 million received from the offering of the 9 7/8% senior notes were deposited into a segregated escrow account.

On December 6, 2010, PAETEC Holding completed its acquisition of Cavalier by merger. Upon the effectiveness of the merger and the satisfaction of other conditions, PAETEC Holding assumed PAETEC Escrow s obligations and agreements in respect of the 9 7/8% senior notes and under the indenture governing such notes, and the escrow arrangements were terminated and the proceeds of the offering of the 9 7/8% senior notes were disbursed from the escrow account and used, together with cash on hand of PAETEC Holding and Cavalier, to pay the consideration and other costs and expenses related to the merger.

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

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

This unaudited pro forma financial information is based on PAETEC management s estimates of fair values of acquired property and equipment and intangible assets. Definitive allocations will be finalized based upon valuations and other studies that were performed following the closing date of the merger. Accordingly, the depreciation and amortization adjustments are preliminary and have been made solely for the purpose of providing unaudited pro forma condensed combined financial information and are subject to revision based on a final determination of fair value. Final determinations of fair value may differ materially from those presented. The unaudited pro forma condensed combined statement of operations also includes certain purchase accounting adjustments, including items expected to have a continuing impact on the combined results, such as interest expense on PAETEC s $450 million offering of the 9 7/8% senior notes completed on December 2, 2010.

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

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

Table of Contents

Unaudited Pro Forma Condensed Consolidated Statement of Operations

For the Year Ended December 31, 2010

(in thousands, except share and per share data)

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

Table of Contents

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

Table of Contents

MANAGEMENT S DISCUSSION AND ANALYSIS OF

FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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

Overview

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

Business Acquisitions

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

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

Indebtedness

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

Table of Contents

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

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

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

Trends Affecting Our Business

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

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

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

Table of Contents

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

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

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

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

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

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

Revenue

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

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

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

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

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

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

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

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

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

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

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

State regulatory commissions historically have regulated the intrastate access rates imposed by incumbent carriers, but many states had subjected the intrastate access rates of competitive carriers to significantly less regulation. A limited number of states in PAETEC s geographic markets have always required competitive

Table of Contents

carriers to mirror the intrastate access rates of the incumbent carrier in that state or mirror interstate rate levels. In recent years, however, several states have implemented new laws or adopted new regulations that limit the intrastate access rates of competitive carriers. Massachusetts, Michigan, New Jersey and Illinois have

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

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

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

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

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

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

Cost of Sales

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

Selling, General and Administrative Expenses

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

Impairment Charge

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

39

Table of Contents

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

Depreciation and Amortization

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

Acquisition, Integration and Separation Costs

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

Debt Extinguishment and Related Costs

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

Interest Expense

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

Other Income, Net

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

Accounting for Income Taxes

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

Stock-Based Compensation

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

Table of Contents

Adjusted EBITDA Presentation

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

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

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

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

including significant differences in the depreciable lives of similar assets among various companies. Adjusted EBITDA facilitates company-to-company comparisons in the communications industry by eliminating some of the foregoing variations. Management believes that because of the variety of equity awards used by companies, the varying methodologies for determining both stock-based compensation and stock-based compensation expense among companies and from period to period, and the subjective assumptions involved in those determinations, excluding stock-based compensation from adjusted EBITDA enhances company-to-company comparisons over multiple fiscal periods. By permitting investors to review both the GAAP and non-GAAP

Table of Contents

measures, PAETEC and its peers that customarily use similar non-GAAP measures facilitate an enhanced understanding of historical financial results and enable investors to make more meaningful company-to-company comparisons.

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

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

- adjusted EBITDA does not reflect PAETEC s capital expenditures, future requirements for capital expenditures or contractual commitments to purchase capital equipment;

- adjusted EBITDA does not reflect the interest expense, or the cash requirements necessary to service interest or principal payments, associated with PAETEC s indebtedness;

- although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will likely have to be replaced in the future, and adjusted EBITDA does not reflect any cash requirements for such replacements;

- adjusted EBITDA does not reflect the cost of equity awards to employees;

- adjusted EBITDA excludes some items in addition to stock-based compensation that are likely to recur;

- adjusted EBITDA does not reflect the effect of earnings or charges resulting from matters that PAETEC s management considers not indicative of PAETEC s ongoing operations; and

- to the extent that PAETEC changes its accounting of certain transactions or other items from period to period, PAETEC s adjusted EBITDA may not be directly comparable from period to period.

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

Results of Operations

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

February 8, 2008.

Table of Contents

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

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

* Less than one percent.

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

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

(3) Exclusive of operating items shown separately below.

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

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

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

45

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

2010 Compared With 2009

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

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

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

Interest Expense. PAETEC s average outstanding debt balances increased to $1,019.4 million for 2010 from $941.2 million for 2009, as a result of the December 2010 issuance of $450 million aggregate principal amount of the 9 $^{7}/8$% senior notes subject to the exchange offer covered by this prospectus and the January 2010

Table of Contents

issuance of $300 million aggregate principal amount of its 8 $^{7}/8$% senior secured notes, which was partially offset by the repayment of the outstanding loans under its senior secured credit facilities from the proceeds of the 8 $^{7}/8$% senior secured notes issuance. Interest expense increased to $96.3 million for 2010 from $74.1 million for 2009 due primarily to an increase in the average outstanding debt balances and an increase in the average annual borrowing rate. The weighted average annual borrowing rate, including the amortization of the debt discount and debt premium but excluding the amortization of deferred financing costs, for 2010 was 9.1%, compared to 7.7% for 2009.

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

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

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

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

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

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

As of December 31, 2010, PAETEC had federal NOL carryforwards of approximately $1.3 billion, including approximately $262.9 million of NOL carryforwards acquired as part of the December 6, 2010 acquisition of Cavalier. PAETEC has recorded a deferred income tax asset of approximately $519.8 million reflecting the benefit of federal and state loss carryforwards. If unused, the NOL carryforwards would expire on various dates from 2016 through 2030. Included in the NOL carryforward deferred tax asset above is approximately $457.4 million of deferred tax assets attributable to federal NOLs and $62.4 million of deferred tax assets attributable to state NOLs. In recognition of the uncertainties relative to the utilization of the NOLs, a full valuation allowance has been recorded.

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

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

2009 Compared With 2008

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

Table of Contents

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

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

Critical Accounting Policies

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

Cost of Sales. Costs of sales are composed primarily of network costs, which are costs incurred for leased transport charges and for transmission of voice and data services over other carriers networks. These costs consist of both fixed payments and variable amounts based on actual usage and negotiated or regulated contract rates. PAETEC expenses network costs as incurred. These costs include PAETEC s estimate of charges for which it has not yet received bills, and are based upon the estimated number of transmission lines and facilities PAETEC has in service and its estimated minutes of use based on internal reports. Once PAETEC receives an invoice from a carrier, the company begins a process of reconciling that carrier s invoice to PAETEC s internal reports. Once the reconciliation is complete, PAETEC follows contractual terms to dispute any erroneous billing and, ultimately, agrees with the carrier on the final amount due. In some cases, this reconciliation process can take several months to complete. PAETEC may make subsequent adjustments to its estimates after it receives bills for the actual costs it incurs, but PAETEC generally does not expect that these adjustments will be material

Table of Contents

to its operating results. Accordingly, PAETEC s accrual for network costs includes estimates for which the reconciliation of the carriers invoices to PAETEC s internal reports has not been completed. Because of the significance of access costs, the complexity of the systems that capture accrual information, and the quantity of negotiated and regulated rates, PAETEC believes that the estimation of network cost accruals is a critical accounting policy. As of December 31, 2010 and 2009, PAETEC had $36.2 million and $27.8 million, respectively, of disputed network invoices and approximately $4.7 million and $8.1 million, respectively, of recorded reserves related to disputed balances recorded in accounts payable on the consolidated balance sheets. As of March 31, 2011, PAETEC had approximately $34.9 million of disputed network invoices and approximately $4.5 million of recorded reserves related to that disputed balance recorded in accounts payable on the consolidated balance sheet.

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

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

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

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

Goodwill is assessed for impairment at least annually using a two-step impairment test. Step one of the test is used to identify whether or not impairment may exist. In step one, PAETEC compares the fair value of each individual reporting unit with its carrying amount. PAETEC estimates the fair value of its reporting units based on the income approach, using a discounted projection of future cash flows, supported with a market-based valuation. The income approach is dependent on a number of critical management assumptions, including estimates of future cash flows that take into account assumed growth rates, price increases, profitability margins, capital expenditures, benefits of recent acquisitions and expected synergies, and an appropriate discount rate. PAETEC s estimates of discounted cash flows may differ from actual cash flows due to, among other factors, economic conditions, changes to PAETEC s business model or changes in operating performance. Significant differences between these estimates and actual cash flows could materially affect PAETEC s future financial results. If a reporting unit s carrying amount exceeds its fair value, impairment may exist. Step two of the impairment test must then be performed to measure the amount of impairment, if any. Goodwill impairment

Table of Contents

potentially exists when the implied fair value of a reporting unit s goodwill is less than its carrying value. ASC 350 requires PAETEC to determine the implied fair value of goodwill in the same manner as if PAETEC had acquired those reporting units. Specifically, PAETEC allocates the fair value of the reporting unit to the assets, including any unrecognized intangible assets, and liabilities of that reporting unit, in a hypothetical calculation that yields the implied fair value of the goodwill. If the carrying amount of the reporting unit s goodwill is greater than the implied fair value of its goodwill, an impairment loss must be recognized for the excess.

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

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

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

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

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

55

Table of Contents

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

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

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

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

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

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

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

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

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

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

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

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

Liquidity and Capital Resources

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

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

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

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

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

Table of Contents

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

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

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

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

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

Net cash provided by financing activities of $438.8 million for 2010 was primarily related to the January 2010 issuance and sale of $300.0 million aggregate principal amount of the 8 7/8% senior secured notes and the December 2010 issuance and sale of $450 million aggregate principal amount of the 9 7/8% senior notes subject to the exchange offer covered by this prospectus by a wholly-owned subsidiary of PAETEC Holding and the subsequent assumption by PAETEC Holding of the subsidiary s obligations and agreements in respect of the 97/8% senior notes. The effects of these note issuances were partially offset by the payment of debt issuance costs incurred in connection with each sale. See Indebtedness below for information about the application of the proceeds of these note issuances. Net cash used in financing activities of $44.1 million for 2009 was primarily related to the repayment of $330.5 million aggregate principal amount of borrowings under PAETEC s senior secured credit facilities with the proceeds of its June 2009 offering of $350 million aggregate principal amount of its 8 7/8% senior secured notes, the payment of debt issuance costs incurred in connection with such sale, and the repayment of $20.0 million aggregate principal amount of loans outstanding under PAETEC s revolving credit facility. Net cash provided by financing activities for 2008 of $127.8 million was primarily related to $100 million of borrowings incurred under PAETEC s incremental term loan facility, a portion of which was applied toward the redemption of McLeodUSA s outstanding senior secured notes in connection with the McLeodUSA acquisition, and $50.0 million of borrowings under PAETEC s revolving credit facility.

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

Table of Contents

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

Contractual Obligations

(in thousands)

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

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

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

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

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

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

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

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

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

Table of Contents

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

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

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

Recently Issued Accounting Standards

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

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

Quantitative and Qualitative Disclosures about Market Risk

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

Management s Annual Report on Internal Control Over Financial Reporting

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

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

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

Management conducted an evaluation of the effectiveness of the system of internal control over financial reporting based on the framework in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commissions (the COSO Framework). Based on this evaluation, management concluded that the Company s system of internal control over financial reporting was effective as of December 31, 2010, based on the COSO Framework. Management has excluded from the scope of its assessment of internal control over financial reporting the operations and related assets of U.S Energy Partners LLC (U.S. Energy), Quagga Corporation (Quagga), and Cavalier Telephone Corporation and its subsidiaries (collectively, Cavalier), which the Company acquired on February 28, 2010, June 7, 2010 and December 6, 2010, respectively. At December 31, 2010 and for the period from March 1, 2010 through December 31, 2010, total assets and total revenues subject to U.S. Energy s internal control over financial reporting represented 0.7% and 1.5% of the Company s consolidated total assets and consolidated total revenues, respectively, as of December 31, 2010 and for the year ended December 31, 2010. At December 31, 2010 and for the period from June 8, 2010 through December 31, 2010, total assets and total revenues subject to Quagga s internal control over financial reporting represented 2.1% and 1.3% of the Company s consolidated total assets and consolidated total revenues, respectively, as of December 31, 2010 and for the year ended December 31, 2010. At December 31, 2010 and for the period from December 6, 2010 through December 31, 2010, total assets and total revenues subject to Cavalier s internal control over financial reporting represented 28.3% and 1.4% of the Company s consolidated total assets and consolidated total revenues, respectively, as of December 31, 2010 and for the year ended December 31, 2010.

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

PAETEC Holding Corp.

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

BUSINESS

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

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

PAETEC s Business

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

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

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

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

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

Network Services

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

Table of Contents

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

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

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

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

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

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

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

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

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

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

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

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

Table of Contents

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

Carrier Services

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

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

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

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

Integrated Solutions

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

Table of Contents

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

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

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

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

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

PAETEC s Network Architecture and Deployment

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

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

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

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

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

Inc. PAETEC also has relationships with providers to supply alternative types of last mile connectivity to certain

Table of Contents

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

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

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

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

Table of Contents

Geographic Markets

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

Sales and Marketing

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

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

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

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

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

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

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

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

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

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

Table of Contents

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

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

Back Office Systems

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

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

Acquisitions

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

- to increase its penetration of PAETEC s existing markets;

- to expand into new markets;

- to augment the geographic scope of PAETEC s network fiber-based assets, primarily in high density markets; and

- to enhance PAETEC s ability to sell and deliver value-added services.

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

Subsidiary Reorganization

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

71

Table of Contents

Competition

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

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

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

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

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

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

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

wireless carriers; and

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

72

Table of Contents

Cable Television Companies

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

Internet Service Providers

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

VoIP Providers

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

Wireless Service Providers

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

In the last few years, consolidation within the wireless industry has resulted in significant growth for the largest wireless providers. Wireless Holdings, Inc. and Sprint Nextel, together with a group of cable television

Table of Contents

operators and information technology companies, recently made major investments in Clearwire Corp. Continued consolidation within the wireless industry could further enhance the economies of scale that would improve the competitiveness of wireless service providers in the telecommunications market.

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

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

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

Regulation

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

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

Table of Contents

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

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

Federal Regulation

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

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

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

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

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

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

- permit competitors to collocate their equipment on the premises of the incumbent carriers at cost-based rates and on a nondiscriminatory basis;

- allow competitors to make use of designated elements of incumbent carrier networks on an unbundled basis, and on non-discriminatory, cost-based rates, in combination with or separate from other wholesale or special access services purchased from the incumbent; and

- offer wholesale versions of their retail telecommunications services for resale at discounted rates.

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

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

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

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

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

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

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

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

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

Table of Contents

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

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

Special Access Regulatory Regime

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

TELRIC Proceeding

A proceeding was initiated at the FCC in 2003 to examine the current rules governing the methodology by which state regulatory authorities set wholesale prices for UNEs, including UNE digital T1 loops, and for collocation, interconnection and intercarrier compensation provided by incumbent carriers to competitive carriers. If the FCC adopts significant changes to the pricing methodology, incumbent carriers could seek approval from state regulatory commissions to increase their prices for a variety of wholesale services required by PAETEC to provide service to its customers. Such an event could raise the cost of doing business for competitive carriers such as PAETEC. We cannot predict whether the FCC will change its pricing rules, or, if it does so, the extent to which state regulatory commissions will permit incumbent carriers to increase their UNE prices.

Qwest and Verizon Dominant Carrier Forbearance Proceedings

Under the Telecommunications Act of 1996, the RBOCs can petition the FCC to forbear from applying regulations implementing the Act. All of the RBOCs have used the provision to secure deregulation of certain services. Qwest and Verizon have petitioned the FCC on multiple occasions to have the FCC forbear from enforcing the unbundling rules in various markets. In June 2010, the FCC denied the second Qwest petition for forbearance in Phoenix filed in March 2009. In rejecting the Qwest petition, the FCC used a market power test, under which the FCC separately analyzed Qwest s market power in different market segments, such as residential retail, enterprise retail and wholesale. Qwest appealed the denial to a federal appellate court, where the matter remains pending. If the court overturns the FCC s use of a market power test, or remands the denial of forbearance back to the FCC for further consideration, or the FCC upholds or grants any forbearance or similar petitions filed by incumbent carriers in the future affecting markets in which PAETEC operates, PAETEC s

Table of Contents

ability to purchase wholesale network services from these carriers at cost-based prices that would allow PAETEC to achieve its target profit margins in those markets could be materially adversely affected. The grant of these petitions also would enable incumbent carriers to compete with their competitors, including PAETEC, more aggressively on price in the affected markets.

Intercarrier Compensation

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

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

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

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

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

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

State Regulation

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

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

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

Some of the states in which PAETEC operates require public utility commission approval before the transfer of a carrier s authority to operate within the state, the transfer of its assets to a new entity, or a change in the control of an entity that controls a carrier operating within the state. Some states also regulate a carrier s issuance of securities, incurrence of debt, guarantees or pledges of security in support of such debt. These requirements can delay and increase the cost we incur to complete various financing transactions, including future stock or debt offerings, the sale of part or all of our regulated business, or the acquisition of assets and other entities to be used in our regulated business.

Local Regulation

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

Intellectual Property

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

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

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

Employees

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

Properties

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

Table of Contents

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

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

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

Legal Proceedings

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

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

MANAGEMENT

Executive Officers and Directors

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

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

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

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

Director qualifications:

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

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

Director qualifications:

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

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

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

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

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

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

Table of Contents

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

Director qualifications:

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

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

Director qualifications:

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

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

Director qualifications:

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

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

Director qualifications:

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

Table of Contents

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

Director qualifications:

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

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

Director qualifications:

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

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

Director qualifications:

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

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

86

Table of Contents

Director qualifications:

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

Board of Directors

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

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

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

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

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

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

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

Table of Contents

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

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

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

Compensation of Directors

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Table of Contents

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

2010 Director Compensation Table

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

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

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

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

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

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

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

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

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

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

Table of Contents

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

2010 Director Equity Awards Table

Name	Date of Grant[1]	Option Awards Stock Options Awarded (#)	Grant Date Fair Value ($)	Date of Grant	Stock Awards Restricted Stock Units Awarded (#)	Grant Date Fair Value ($)
Richard T. Aab	2/23/2010	10,500	28,044	2/23/2010	10,500	41,055
Shelley Diamond	2/23/2010	8,500	22,703	2/23/2010	8,500	33,235
Shelley Diamond	5/27/2010	1,000	2,873	5/27/2010	1,000	4,220
H. Russell Frisby, Jr.	2/23/2010	8,500	22,703	2/23/2010	8,500	33,235
Tansukh V. Ganatra	2/23/2010	9,500	25,374	2/23/2010	9,500	37,145
Michael C. Mac Donald	2/23/2010	9,500	25,374	2/23/2010	9,500	37,145
Michael C. Mac Donald	5/27/2010	5,500	15,799	5/27/2010	5,500	23,210
William R. McDermott	2/23/2010	10,500	28,044	2/23/2010	10,500	41,055
Alex Stadler	2/23/2010	7,500	20,032	2/23/2010	7,500	29,325
Alex Stadler	5/27/2010	1,000	2,873	5/27/2010	1,000	4,220
Mark Zupan	2/23/2010	12,500	33,386	2/23/2010	12,500	48,875

(1) Additional awards issued on May 27, 2010 reflect awards made to directors appointed to the newly-formed nominating and governance committee and, in the case of Mr. Mac Donald, also appointed as the Lead Director.

Compensation Discussion and Analysis

The purpose of this Compensation Discussion and Analysis is to provide material information about our compensation philosophy, objectives, programs and policies and to explain to our stockholders how we arrived at the levels and forms of compensation that were earned by or paid to the executive officers identified in the Summary Compensation Table under Executive Compensation for their service in 2010. We describe not only what we pay these named executive officers, but also why and how we link their compensation to our business results.

Compensation Philosophy and Objectives

Our executive compensation programs and policies are intended to promote and sustain profitable growth in the dynamic business environment in which PAETEC operates.

We seek to design and administer our executive compensation plans and programs in alignment with a number of central objectives, which are to:

- complement and support PAETEC s mission to be the most customer- and employee-oriented communications provider, and advance our corporate values, which include a caring culture, open communication, unmatched service and personalized solutions;
- promote relative consistency and balance in the components of compensation across all levels of our employees;
- attract and retain high-quality executives through programs that are competitive within the telecommunications industry;
- tie a significant portion of our executives overall compensation to key short-term and long-term strategic, financial and operational goals;

align the interests of our executives with those of our stockholders through a philosophy that provides considerable opportunity for above-target performance and downside risk if performance goals are not achieved; and

provide compensation programs that are financially efficient, affordable and sustainable.

We believe that encouraging executives to think and act like owners aligns to a significant degree the interests of our management with the interests of our long-term stockholders.

Setting of Executive Compensation

In determining the levels and forms of compensation paid to the named executive officers for 2010, the compensation committee considered measures of company performance, measures of individual executive performance and experience, and internal equity with respect to positions within the same level (such as senior vice president or executive vice president). The committee reviewed executive compensation tally sheets for each of the named executive officers prepared by its consultant to gain a comprehensive view of the total compensation paid or payable to each executive. We discuss below under Elements of Compensation the compensation decisions for the named executive officers for 2010.

In evaluating and structuring PAETEC s executive compensation program for 2010, the compensation committee also considered the competitive market for comparable executives and compensation opportunities provided by comparable companies. To assist it in these determinations, the committee engaged an outside consultant, First Niagara Benefits Consulting Group, to provide benchmark and market data for each individual element of executive compensation, as well as for total compensation levels. The consultant provided data to assist the committee in understanding how PAETEC s executive compensation compared to the executive compensation paid by its market competitors. The committee compared PAETEC s actual compensation paid, as well as its executive compensation elements and practices generally, with the compensation paid and executive compensation elements and practices of a selected comparison group of public companies.

During 2010, with the assistance of its consultant, the compensation committee conducted a review of the composition of the comparison group of companies it had established in the previous year when fixing executive compensation for 2009. The review of the comparison group took into account continuing consolidation and other changes within the telecommunications industry and the size and complexity of PAETEC s operations. The committee concluded that the current mix of communications services companies and comparably-sized companies that are principally engaged in technology and non-manufacturing services was appropriate. For 2010, the following companies were included in the compensation comparison group:

3Com Corporation	Global Crossing Limited
ADC Telecommunications, Inc.	Leap Wireless International, Inc.
Arris Group, Inc.	Level 3 Communications, Inc.
Belo Corp.	Mediacom Communications Corp.
CenturyTel, Inc.	MetroPCS Communications, Inc.
Cincinnati Bell Inc.	The Dun & Bradstreet Corp.
Compuware Corporation	tw telecom inc.
Earthlink, Inc.	Windstream Corporation
Frontier Communications Corporation	XO Holdings, Inc.
Hughes Communications Inc.	

The committee s consultant provided detailed compensation data for the named executive officers in the compensation comparison group, aggregate data for the group, and information on compensation practices across the group. The committee intends to continue to review the composition of the peer group annually to ensure that it accurately reflects the overall competitive marketplace for PAETEC executive compensation.

The consultant also prepared and presented the committee with data from national survey sources, including Watson Wyatt Data Services, Mercer Human Resources, and the Economic Research Institute, using, to the extent reasonably possible, reported data from the telecommunications industry for organizations having comparable revenue and size of employee base.

The committee used the comparison group information to target specifically a desired level of each element of compensation payable to the named executive officers. We discuss these specific targets below. The committee used the general survey data to support further its benchmark for each element of executive compensation for each of our named executive officers. The committee did not consider the individual companies within the general surveys, but instead focused only on the aggregated compensation data of the survey information.

Elements of Compensation

For 2010, we provided each of the named executive officers and our other executive officers with a total compensation package that included the following three individual elements:

- base salary;
- the potential for an annual cash incentive payment; and
- long-term performance-based and time-based equity incentives.

We strive to provide appropriate levels of fixed versus at-risk compensation and cash versus equity-based compensation relative to each officer s role and responsibilities. Other than our use of the benchmarks described below, however, we do not have any formal policies regarding specified relative levels of these compensation elements.

Our named executive officers are eligible to participate in the same benefit programs we offer to all employees. These plans include medical, dental, life insurance, disability, and qualified 401(k) retirement plans, and a variety of voluntary benefit plans.

Base Salary. Base salary levels during 2010 for our named executive officers generally reflected the external market value of their respective roles and took into consideration the individual s current performance and experience and the scope and complexity of the officer s position within PAETEC. Executive officers do not receive automatic annual merit increases in base salary. The committee annually reviews base salary for executive officers and makes adjustments it deems to be appropriate based on market comparisons, performance and internal equity with respect to positions within the same level.

The committee believes that, for PAETEC s executive compensation to remain competitive with the market, the desired market position for base salary generally is to achieve approximately the 50^{th} percentile of the comparison group and general survey data. In February 2010, the committee reviewed an analysis prepared by its consultant of the competitiveness of the base salaries for the named executive officers. The committee decided to maintain base salaries at 2009 levels for service in 2010, even though the 2009 base salary levels were generally lower than the 50^{th} percentile of the comparison group and companies represented in the general survey data. Although the committee was satisfied with Mr. Chesonis s performance and Mr. Chesonis was satisfied with the individual performance of the other named executive officers, the committee concluded that total compensation, including annual and long-term incentives, was fair and competitive with compensation disclosed in the market data.

Annual Incentive Cash Compensation. Annual incentive compensation at PAETEC is intended to reward employees for the achievement of specific key performance objectives identified as having the potential for a positive effect on our annual business results. The committee believes that the desired market position for annual incentive compensation generally is to pay approximately the market median for the achievement of targeted results, and to pay above the market median for the achievement of results that exceed the targets.

Table of Contents

The bonus payment for the named executive officers under our annual cash bonus plan is determined in four steps:

1. Bonus plan funding is based on PAETEC s achievement of performance targets for the fiscal year and is expressed as a plan funding percentage.

2. Each named executive officer is assigned a predetermined individual bonus award target, which is expressed as a percentage of eligible base salary. The individual bonus targets for 2010 are shown below.

3. The standard bonus percentage is calculated by multiplying the individual bonus target by the 2010 plan funding percentage.

4. The standard bonus percentage then may be subject to a potential increase or decrease from the individual target based on the CEO s recommendation and the committee s assessment of the participant s performance toward individual, departmental or company-wide goals, except that the CEO s percentage may not be increased.

2010 Bonus Plan. The 2010 individual bonus award targets for each named executive officer, which were based on the executive s responsibility level within PAETEC and an analysis of the comparison group and general survey data, were set as follows:

Position	Target % of Salary
Chief Executive Officer	75
Chief Financial Officer	75
President of PAETEC s Energy Business	75
President National Sales & Service	50
Chief Information Officer	50
General Counsel & Secretary	40
Senior Vice President Human Resources	40

The funding of the bonus plan for 2010 was based on PAETEC s operating results for fiscal 2010. Payout under the 2010 bonus plan was based on performance measured against the following metrics:

40% based on adjusted EBITDA;

40% based on revenue; and

20% based on customer satisfaction (net promoter score).

Adjusted EBITDA is not a measurement of financial performance under accounting principles generally accepted in the United States of America, or GAAP, and is considered a non-GAAP financial measure under the SEC s rules. As defined by PAETEC for purposes of its bonus plan, adjusted EBITDA represents net (loss) income before interest, taxes, depreciation and/or amortization, non-cash compensation expense, income from discontinued operations, gain on cancellation of debt, restructuring and/or integration charges and costs, reorganization and/or recapitalization items, impairment charges, and gain on non-monetary transaction, as further adjusted to exclude the following: asset write-downs; litigation or claim judgments or settlements; the effect of changes in tax laws, accounting principles, or other laws or provisions affecting reported results; any reorganization and restructuring programs; extraordinary nonrecurring items as described in Accounting Standards Codification Topic 225, *Income Statement*, and/or in management s discussion and analysis of financial condition and results of operations appearing in PAETEC s annual report to stockholders for the applicable year; acquisitions or divestitures; and foreign exchange gains or losses.

The revenue metric reflected the importance of a continued focus on sales in light of the increased size and complexity of our operations.

Table of Contents

PAETEC measures customer satisfaction using the net promoter score survey methodology, which is commonly used in the telecommunications industry. The survey is administered by a third-party firm and measures the likelihood that the customer would recommend PAETEC as a communications provider.

The plan provided for the funding of the bonus pool on a pro-rata basis based on achievement against threshold, target and stretch goals for each of the plan performance metrics.

To determine funding for the 2010 bonus plan pool, the committee considered the performance targets and actual results shown below:

Plan Performance Metric	Threshold	Target	Stretch	Actual Results
Adjusted EBITDA	$ 265.0 million	$ 275.0 million	$ 290.0 million	$ 264.9 million
Revenue	$ 1,600.0 million	$ 1,620.0 million	$ 1,720.0 million	$ 1,623.8 million
Customer satisfaction	18.8	20.7	22.7	13.4

Because we did not achieve all of the threshold performance targets for 2010, Mr. Chesonis did not recommend, and the committee did not approve, the payment of an annual bonus based on 2010 performance for any of the named executive officers. In addition, the committee did not approve the payment of an annual bonus for Mr. Chesonis. Accordingly, no amounts are shown for 2010 in the non-equity incentive plan compensation column of the 2010 Summary Compensation Table under Executive Compensation following this Compensation Discussion and Analysis. Although we did not pay any amounts under our 2010 bonus plan, we are obligated to make a bonus payment of $247,500 to Edward J. Butler, Jr., in connection with the termination of his employment as President of PAETEC s Energy Business effective on November 5, 2010. For further information about this payment see Termination and Change of Control Payments Actual Payment Obligations to Former Named Executive Officer under Executive Compensation following this Compensation Discussion and Analysis.

2011 Bonus Plan. The cash bonus plan for 2011 for the Company s named executive officers will be based on performance measured against the following metrics: 40% based on adjusted EBITDA (defined as described above); 40% based on revenue; and 20% based on customer satisfaction (net promoter score).

The 2011 individual bonus award targets for our named executive officers are set forth below:

Position	Target % of Salary
Chief Executive Officer	75
Chief Operating Officer	75
Chief Financial Officer	75
Chief Information Officer	50
President National Sales & Service	50
General Counsel & Secretary	50

All of the performance measures for the 2011 bonus plan are stockholder-approved performance measures under our 2007 omnibus incentive plan, and, with respect to the CEO, bonus awards payable upon achievement of these performance measures are intended to satisfy the requirements under section 162(m) of the Internal Revenue Code for qualified performance-based compensation.

Long-Term Incentive Compensation. Long-term incentives under our 2007 omnibus incentive plan serve an important role in supporting the compensation program objectives by ensuring that a significant portion of executive compensation is tied to long-term company performance and changes in stockholder value. To support PAETEC s long-term growth objectives, the committee believes that, for its named executive officers and other key executives, PAETEC should provide an opportunity for long-term incentive compensation generally at or above the 75th percentile of the competitive market.

In August 2007, the committee approved in principle a long-term, equity-based incentive program that would focus on achievement of PAETEC s long-term business objectives. The committee reviewed and modified those objectives in December 2009. The current program as reviewed and endorsed by the compensation committee has the following two primary components:

Annual Base Equity Program. This program provides a market level long-term compensation opportunity, assists in the retention of executives and, through its performance-based features, focuses executives on critical performance results. The annual grants of time-based stock options and performance-based restricted stock units, or RSUs, are awarded to our executive officers, with 50% of the shares subject to the grant issuable pursuant to stock options and 50% of the shares issuable pursuant to performance-based RSUs. The stock option awards vest with respect to one-fourth of the shares on each of the first four anniversaries of the grant date. The performance-based RSU awards vest with respect to one-third of the shares on each of the first three anniversaries of the grant date contingent in each year upon our achievement of the performance objective for such year. For awards granted in 2008, 2009 and 2010, the performance objective for the base equity RSU awards is achievement of specified annual levered free cash flow objectives. Levered free cash flow is considered a non-GAAP financial measure under the SEC s rules. For purposes of the base equity program awards, levered free cash flow, as defined by PAETEC, consists of adjusted EBITDA (defined as described above) less capital expenditures (purchases of property, plant and equipment) less interest.

Performance Accelerator Program. This program is intended to reward our executive officers and other key officers with above-market equity compensation for the achievement of performance goals considered exceptional and significant. The awards are performance-based grants of RSUs and vest with respect to one-fourth of the shares on each of the first four anniversaries of the grant date contingent upon the achievement of the specified performance goal during the first year of the award. For awards granted in 2008, 2009 and 2010, the performance goal for the performance accelerator RSU award was achievement of a specified increase in PAETEC s stock price during the first year of the award.

2010 Grants Under Annual Base Equity Program. The compensation committee approved grants under the annual base equity program in March 2010 for each of our named executive officers other than Mr. Wilson and Mr. Butler, and in May 2010 for Mr. Butler and Mr. Wilson. Of each grant, 50% of the shares awarded are issuable pursuant to a grant of stock options and 50% of the shares awarded are issuable pursuant to a grant of performance-based RSUs. The stock option awards vest with respect to one-fourth of the shares on each of the first four anniversaries of the grant date. The performance-based RSU awards vest with respect to one-third of the shares on each of the first three anniversaries of the grant date contingent each year upon the achievement of an annual levered free cash flow objective for such year. The levered free cash flow target for 2010 was set at $38.2 million, which the company exceeded. As a result, the first third of the awards granted in 2010 vested in March 2011 or, with respect to the awards to Mr. Butler and Mr. Wilson, will vest in May 2011. The levered free cash flow targets for 2010, 2011 and 2012 were set at levels that were considered to be challenging, but reasonably likely to be achieved based on PAETEC s recent operating trends.

Vesting of 2009 and 2008 Grants Under Annual Base Equity Program. The second tranche of the annual base equity awards granted in 2009 contained a 2010 levered free cash flow target of $44.1 million, which the company exceeded. Accordingly, this tranche vested in March 2011. The third and final tranche of the annual base equity awards granted in 2008 contained a 2010 levered free cash flow target of $59.9 million, which was not achieved. Accordingly, this tranche was cancelled in March 2011.

2010 Grants Under Performance Accelerator Program. The compensation committee also approved grants of performance-based RSUs under the performance accelerator program for 2010 in March 2010 for each of our named executive officers other than Mr. Wilson and Mr. Butler, and in May 2010 for Mr. Butler and Mr. Wilson. Vesting of the awards was conditioned upon the achievement of a 10% increase in the PAETEC stock price in the 12 months following the award. Because the target was not achieved, the awards were cancelled in March 2011 or, with respect to the awards to Mr. Butler and Mr. Wilson, will be cancelled in May 2011.

Table of Contents

For further information about the equity grants in 2010 discussed above, see the 2010 Grants of Plan-Based Awards Table under Executive Compensation following this Compensation Discussion and Analysis.

Perquisites and Other Benefits. PAETEC does not offer perquisites or significant benefits to our named executive officers that are not otherwise available to all of our employees. We also do not currently provide our executive officers with pension arrangements, post-retirement health coverage, non-qualified deferred compensation arrangements, or other similar benefits.

Stock Ownership and Retention Policy

In July 2009, the committee adopted an officer stock ownership and retention policy intended to ensure a strong alignment between the interests of management and our stockholders. This policy requires that covered executives beneficially own and retain at least 50% of each equity award, on a net basis after the payment of taxes, for a period of 36 months from the vesting of each equity award granted after the implementation of the policy. This policy applies to all of our named executive officers.

Timing of Equity Awards

The grant date of equity awards for our executive officers is either the date of the compensation committee meeting at which the award determinations are made or a specified date after the compensation committee approval date. Because the compensation committee may take action to approve equity awards on or near the date that PAETEC s annual or quarterly earnings are released, the compensation committee in these circumstances generally will provide that the second business day after the release will be the grant date to ensure that the earnings results are absorbed by the market before equity awards are granted and stock option exercise prices are established. In other circumstances, however, PAETEC could grant options or other equity awards to executive officers and other employees while material developments have not been disclosed. The compensation committee could, for example, grant awards in advance of announcing an acquisition or other corporate transaction, as a retention tool or to provide an incentive to accomplish the transaction. The exercise price of stock options issuable under our 2007 omnibus incentive plan is the closing price of our common stock as reported on the NASDAQ Global Select Market on the grant date.

Severance and Change of Control Arrangements

Severance and change of control arrangements give the company the flexibility to make changes in key executive positions, if changes are determined by the board of directors to be in our best interests. We consider these arrangements to be particularly important in situations involving a possible change of control of our company because they can help to secure the dedicated attention of executive officers whose personal positions are at risk in such situations and who may have other opportunities available to them. By establishing compensation and benefits payable under various merger and acquisition possibilities, the change of control provisions help to minimize distractions arising out of the officer s concern over personal financial and career prospects and promote continuity of the leadership team at a time when business continuity is of paramount concern to our company.

Before 2008, we maintained a senior officer confidentiality, non-solicitation, non-competition and severance agreement with each senior officer, including our named executive officers. On February 22, 2008, we entered into new agreements with each executive officer, including each named executive officer, which more closely reflect current competitive practices relating to severance arrangements. Upon the effectiveness of the new agreements, the previous agreements between PAETEC and the executive officers were terminated. Among other provisions, the new agreements, as compared to the prior agreements, provide for reduced cash severance payments upon the termination of the executives employment in specified circumstances, limit the circumstances in which equity-based awards granted during the employment term will continue to vest following termination of employment, and increase the scope of the post-termination non-solicitation and non-competition covenants to which the executives are subject. These agreements also require the executive to provide us with a general release of claims against the company and our affiliates. The agreements for five of our named executive officers, Mr. Chesonis, Mr. DeRiggi, Mr. Moore, Ms. O Connell and Ms. Zaucha, were revised on March 26, 2010 to reduce the amount of cash severance payable upon any voluntary termination of their employment by these officers. In addition, on January 1, 2011, Ms. O Connell entered into the form of severance agreement applicable to certain executive vice presidents of PAETEC, which superseded her prior agreement applicable to certain senior vice presidents of PAETEC.

For a more detailed discussion of our severance agreements, including information regarding the amounts that would have been payable to each named executive officer if a payment triggering event had occurred on December 31, 2010, see Termination and Change of Control Payments under Executive Compensation following this Compensation Discussion and Analysis.

Compensation Deductibility

Section 162(m) of the Internal Revenue Code generally limits to $1 million per person PAETEC s tax deduction of certain non-performance-based compensation paid in a given year to PAETEC s principal executive officer and three most highly compensated officers (other than the principal financial officer).

The levels of non-performance-based salary, bonus and other compensation paid by PAETEC typically do not exceed the $1 million cap for our executive officers. As discussed above and as a matter of practice, with respect to the CEO, the committee intends to set performance-based goals annually under PAETEC s various variable compensation plans and for PAETEC to deduct compensation paid under these plans and gains realized from stock options to the extent consistent with the provisions of section 162(m). The committee may conclude, however, that paying non-deductible compensation is consistent with our stockholders best interests for certain events.

Accounting Considerations

In structuring equity-based awards, the compensation committee considers the accounting impact under ASC 718, *Compensation-Stock Compensation,* of granting such awards. ASC 718 requires the measurement of the cost of employee services received in exchange for an award of equity instruments based on the grant-date fair value of the award. The cost will be recognized over the period during which an employee is required to provide service in exchange for the award.

Table of Contents

Executive Compensation

Summary Compensation Information

The following summary compensation table presents information about compensation that was earned by or paid to PAETEC s Chief Executive Officer, Chief Financial Officer, each of our other three most highly compensated executive officers serving with us at December 31, 2010, and two additional individuals who served as executive officers for part of 2010. We refer to these individuals in this proxy statement as the named executive officers. Information is provided only for 2010 for Mario DeRiggi and Mary K. O Connell, each of whom first became named executive officers during that year. The employment with the company of Edward J. Butler, Jr., formerly Executive Vice President and President of PAETEC s Energy Business, terminated on November 5, 2010. The employment with the company of Laurie L. Zaucha, formerly Senior Vice President Human Resources, terminated on March 4, 2011.

Summary Compensation Table

Name and Principal Position	Year	Salary ($)	Bonus ($)(1)	Stock Awards ($)(2)	Option Awards ($)(2)	Non-Equity Incentive Plan Compensation ($)(3)	All Other Compensation ($)(4)	Total ($)
Arunas A. Chesonis	2010	500,000		527,712	157,115			1,184,827
Chairman, President and Chief	2009	500,000		45,335	12,743	363,750		921,828
Executive Officer	2008	500,000		1,294,016	72,075		6,900	1,872,991
Edward J. Butler, Jr.	2010	298,269(5)		117,551	39,374		1,178,842(6)	1,634,036
Executive Vice President and	2009	330,000		45,335	12,743	240,075		628,153
President of PAETEC s Energy Business	2008	330,000		1,127,416	72,075		6,900	1,536,391
Keith M. Wilson	2010	330,000		117,551	39,374			486,925
Executive Vice President and Chief	2009	330,000		45,335	12,743	240,075		628,153
Financial Officer, Treasurer	2008	330,000		1,127,416	72,075		6,900	1,536,391
Robert D. Moore, Jr.	2010	250,000		211,085	62,846			523,931
Executive Vice President and Chief	2009	230,000		60,856	32,711	86,562		410,129
Information Officer	2008	230,000		465,041	33,635		6,900	735,576
Laurie L. Zaucha	2010	250,000		158,314	47,135			455,449
Senior Vice President Human	2009	250,000		21,156	27,184	121,249		419,589
Resources	2008	250,000	112,000	348,421	33,635		6,900	750,956
Mario DeRiggi. *Executive Vice President and President, National Sales and Service*	2010	300,000		211,085	62,846			573,931
Mary K. O Connell *Executive Vice President, General Counsel and Secretary*	2010	250,000		158,314	47,135			455,449

(1) Amount paid for 2008 to Ms. Zaucha represents a signing bonus upon her commencement of employment with PAETEC in November 2007.

(2) Amounts shown in the Stock Awards and Option Awards columns reflect the aggregate grant date fair value of the awards computed in accordance with ASC 718. Assumptions used in the calculation of these amounts, including with respect to performance-based awards, are set forth in Note 9 to PAETEC s audited consolidated financial statements appearing elsewhere in this prospectus.

(3) No Non-Equity Incentive Plan Compensation payments were earned for 2010 because the applicable performance targets for 2010 were not achieved.

(4) The amounts shown consist of matching contributions by PAETEC pursuant to its 401(k) savings and retirement plan. For 2009 and 2010, there were no matching contributions by PAETEC.

(5) Amount shown represents actual salary for 2010 paid to Mr. Butler, whose employment with PAETEC terminated in November 2010.

(6) Amount includes $1,178,842 in salary and benefits continuation and payment in lieu of bonuses paid or accrued by PAETEC in connection with the termination of Mr. Butler s employment in November 2010. For further information, see Termination and Change of Control Payments Actual Payment Obligations to Former Named Executive Officer below.

Grants of Plan-Based Awards

The following table presents information with respect to the grants of plan-based awards by PAETEC to the named executive officers during 2010.

2010 Grants of Plan-Based Awards Table

Name	Grant Date	Action Date[1]	Estimated Future Payouts Under Non-Equity Incentive Plan Awards: Threshold ($)	Target ($)[2]	Maximum ($)[2]	Estimated Future Payouts Under Equity Incentive Plan Awards: Threshold (#)	Target (#)	Maximum (#)	All Other Stock Awards: Number of Shares of Stock or Units (#)	All Other Option Awards: Number of Securities Underlying Options (#)	Exercise or Base Price of Option Awards ($/Sh)	Grant Date Fair Value of Stock and Option Awards ($)[3]
Arunas A. Chesonis				375,000	750,000							
	3/26/10	3/25/10								50,000[4]	4.59	157,115
	3/26/10	3/25/10					50,000[5]					229,500
	3/26/10	3/25/10					100,000[6]					298,212
Edward J. Butler, Jr.				247,500								
	5/25/10	5/25/10								15,000[4]	3.87	39,374
	5/25/10	5/25/10					15,000[7]					58,050
	5/25/10	5/25/10					30,000[8]					59,501
Keith M. Wilson				247,500								
	5/25/10	5/25/10								15,000[4]	3.87	39,374
	5/25/10	5/25/10					15,000[7]					58,050
	5/25/10	5/25/10					30,000[8]					59,501
Robert D. Moore, Jr.				125,000								
	3/26/10	3/25/10								20,000[4]	4.59	62,846
	3/26/10	3/25/10					20,000[5]					91,800
	3/26/10	3/25/10					40,000[6]					119,285
Laurie L. Zaucha				100,000								
	3/26/10	3/25/10								15,000[4]	4.59	47,135
	3/26/10	3/25/10					15,000[5]					68,850
	3/26/10	3/25/10					30,000[6]					89,464
Mario DeRiggi				150,000								
	3/26/10	3/25/10								20,000[4]	4.59	62,846
	3/26/10	3/25/10					20,000[5]					91,800
	3/26/10	3/25/10					40,000[6]					119,285
Mary K. O Connell				100,000								
	3/26/10	3/25/10								15,000[4]	4.59	47,135
	3/26/10	3/25/10					15,000[5]					68,850
	3/26/10	3/25/10					30,000[6]					89,464

(1) On March 25, 2010, the compensation committee approved grants of stock options and restricted stock units effective, subject to specified conditions, on March 26, 2010 to each of the named executive officers other than Mr. Wilson and Mr. Butler. The grants to Mr. Wilson and Mr. Butler were approved by the compensation committee on May 25, 2010.

(2) Amounts represent potential payments to each named executive officer under our annual bonus plan for 2010 if performance targets had been achieved. The bonus plan does not provide for any minimum amounts payable or, except with respect to PAETEC s Chief Executive Officer, maximum amounts payable. The material terms of these incentive awards are described under Compensation Discussion and Analysis.

(3) Represents the grant-date fair value computed in accordance with ASC 718. For a discussion of assumptions used in the 2010 valuations, see Note 9 to PAETEC s audited consolidated financial statements appearing elsewhere in this prospectus.

(4) Reflects an award of stock options that will vest in four equal annual installments beginning on March 26, 2011.

(5) Reflects an award of restricted stock units that will vest in three equal annual installments beginning on March 26, 2011 subject to the achievement of specified performance targets each year. The performance target for the vesting of the first installment was achieved. The material terms of these incentive awards are described under Compensation Discussion and Analysis.

(6) Reflects an award of restricted stock units that will vest in four equal annual installments beginning on March 26, 2011 subject to the achievement of a performance target in the first year. The performance target was not achieved and all of the awards were cancelled on March 26, 2011. The material terms of these incentive awards are described under Compensation Discussion and Analysis.

(7) Reflects an award of restricted stock units that will vest in three equal annual installments beginning on May 25, 2011 subject to the achievement of specified performance targets each year. The performance target for the first installment was achieved. The material terms of these incentive awards are described under Compensation Discussion and Analysis.

(8) Reflects an award of restricted stock units that will vest in four equal annual installments beginning on May 25, 2011 subject to the achievement of a performance target in the first year. The performance target was not achieved and all of the awards will be cancelled on May 25, 2011. The material terms of these incentive awards are described under Compensation Discussion and Analysis.

Table of Contents

Outstanding Equity Awards at Fiscal Year-End

The following table presents information with respect to the outstanding equity awards at 2010 fiscal year-end for the named executive officers.

2010 Outstanding Equity Awards at Fiscal Year-End Table

	Option Awards				Stock Awards			
Name	Number of Securities Underlying Unexercised Options Exercisable (#)	Number of Securities Underlying Unexercised Options Unexercisable (#)	Option Exercise Price ($)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested ($)(1)	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested ($)(1)
Arunas A. Chesonis					115,000(2)	430,100	187,500(3)	701,250
	226,062		2.16	3/26/2012				
	291,223		1.85	4/2/2013				
	7,500	7,500(4)	7.64	3/3/2018				
	3,750	11,250(5)	1.28	3/2/2019				
		50,000(6)	4.59	3/26/2020				
Edward J. Butler, Jr.					95,000(7)	355,300	55,000(8)	205,700
	7,500	7,500(4)	7.64	11/5/2015				
	3,750	7,500(9)	1.28	11/5/2015				
		7,500(10)	3.87	11/5/2015				
Keith M. Wilson					95,000(2)	355,300	82,500(11)	308,550
	591,749		4.01	6/15/2011				
	81,149		1.85	4/2/2013				
	7,500	7,500(4)	7.64	3/3/2018				
	3,750	11,250(5)	1.28	3/2/2019				
		15,000(12)	3.87	5/25/2020				
Robert D. Moore, Jr.					44,500(13)	166,430	77,500(14)	289,850
	15,271		4.01	6/30/2011				
	243		2.16	3/15/2012				
	2,191		2.16	4/30/2012				
	649		1.85	3/15/2013				
	3,471		1.85	4/2/2013				
	243		3.39	3/20/2014				
	24,345		3.39	3/31/2014				
	324		3.86	3/31/2015				
	24,345		1.24	12/29/2015				
	324		1.37	3/15/2016				
	3,500	3,500(4)	7.64	3/3/2018				
	1,750	5,250(5)	1.28	3/2/2019				
	2,500	7,500(15)	3.97	12/9/2019				
		20,000(6)	4.59	3/26/2020				
Laurie L. Zaucha					30,000(2)	112,200	62,500(16)	233,750
	18,750	6,250(17)	9.45	12/19/2017				
	3,500	3,500(4)	7.64	3/3/2018				
	8,000	24,000(5)	1.28	3/2/2019				
Mario DeRiggi					50,000(2)	187,000	85,000(18)	317,900
	81		3.39	3/20/2014				

24,345		3.39	3/31/2014
162		3.86	3/31/2015
10,144		1.24	12/29/15
5,000	5,000(4)	7.64	3/3/2018
2,500	7,500(5)	1.28	3/2/2019
	20,000(6)	4.59	3/26/2020

101

Table of Contents

	Option Awards				Stock Awards			
Name	Number of Securities Underlying Unexercised Options Exercisable (#)	Number of Securities Underlying Unexercised Options Unexercisable (#)	Option Exercise Price ($)	Option Expiration Date	Number of Shares or Units of Stock That Have Not Vested (#)	Market Value of Shares or Units of Stock That Have Not Vested ($)[1]	Equity Incentive Plan Awards: Number of Unearned Shares, Units or Other Rights That Have Not Vested (#)	Equity Incentive Plan Awards: Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested ($)[1]
Mary K. O Connell					23,361[19]	87,370	61,500[20]	230,010
	324		2.16	3/15/2012				
	1,460		2.16	4/30/2012				
	649		1.85	3/15/2013				
	738		1.85	4/30/2013				
	162		2.93	12/17/2013				
	324		3.39	3/20/2014				
	16,230		3.39	3/31/2014				
	324		3.86	3/31/2015				
	4,869		1.24	12/29/2015				
	324		1.37	3/15/2016				
	4.057		1.37	3/30/2016				
	1,500	500[21]	11.93	8/31/2017				
	2,000	2,000[4]	7.64	3/3/2018				
	1,000	1,000[22]	3.56	9/3/2018				
	3,500	3,500[23]	1.29	12/18/2018				
	3,500	10,500[5]	1.28	3/2/2019				
		15,000[6]	4.59	3/26/2020				

(1) Amount shown is determined by multiplying the value of PAETEC s common stock as of December 31, 2010, which was the closing sale price of $3.74 per share as reported on the NASDAQ Global Select Market, by the number of units of stock subject to the restricted stock unit awards.

(2) Of the awards shown, one-half vested on February 22, 2011 and one-half will vest on February 22, 2012.

(3) Of the awards shown, restricted stock units for 5,000 shares awarded on March 3, 2008 were cancelled in March 2011 because the performance target was not achieved. Of the restricted stock units for 22,500 shares awarded on March 2, 2009, one-third vested on March 2, 2011 and the remaining two-thirds will vest in two equal annual installments beginning on March 2, 2012, as the sole performance target was achieved in the first year of the vesting period. Of the restricted stock units for 10,000 shares separately awarded on March 2, 2009, one-half vested on March 2, 2011 and one-half will vest on March 2, 2012 subject to the achievement of a performance target. Of the restricted stock units for 50,000 shares awarded on March 26, 2010, one-third vested on March 26, 2011 and the remaining two-thirds will vest in two equal annual installments beginning on March 26, 2012 subject to the achievement of a performance target in each year of the vesting period. The restricted stock units for 100,000 shares separately awarded on March 26, 2010 were cancelled in March 2011 because the performance target was not achieved.

(4) Of the awards shown, one-half vested on March 3, 2011 and one-half will vest on March 3, 2012.

(5) Of the awards shown, one-third vested on March 2, 2011 and the remaining two-thirds will vest in two equal annual installments on March 2, 2012 and March 2, 2013.

(6) Of the awards shown, one-fourth vested on March 26, 2011 and the remaining three-fourths will vest in three equal annual installments on March 26, 2012, March 26, 2013, and March 26, 2014.

(7) Of the awards shown, one-half vested on February 22, 2011 and one-half will vest on February 22, 2012 subject to compliance with certain conditions in Mr. Butler s severance agreement.

(8) Of the awards shown, restricted stock units for 5,000 shares awarded on March 3, 2008 were subject to a performance target that was not achieved and were cancelled in March 2011. Of the restricted stock units for 15,000 shares awarded on March 2, 2009, one-half vested on March 2, 2011 and one-half will vest on March 2, 2012, as the performance target was achieved in the first year of the vesting period, subject to compliance with certain conditions in Mr. Butler s severance agreement. Of the restricted stock units for 10,000 shares awarded on March 2, 2009, one-half vested on March 2, 2011 and one-half will vest on March 2, 2012 subject to the achievement of a performance target and subject to compliance with certain conditions in Mr. Butler s severance agreement. The restricted stock units for 10,000 shares awarded on May 25, 2010 will vest in two equal annual installments beginning on the first anniversary of the grant date subject to the achievement of a performance target in each year of the vesting period and subject to compliance with certain conditions in Mr. Butler s severance agreement. The performance target for the first installment was achieved, and 5,000 shares of this award will vest in May 2011. The restricted stock units for 15,000 shares separately awarded on May 25, 2010 will be cancelled in May 2011 because the performance target was not achieved.

(9)

Of the awards shown, one-half vested on March 2, 2011 and one-half will vest on March 2, 2012 subject to compliance with certain conditions in Mr. Butler s severance agreement.

(10) The awards shown will vest in two equal annual installments on May 25, 2011 and May 25, 2012 subject to compliance with certain conditions in Mr. Butler s severance agreement.

Table of Contents

(11) Of the awards shown, restricted stock units for 5,000 shares awarded on March 3, 2008 were cancelled in March 2011 because the performance target was not achieved. Of the restricted stock units for 22,500 shares awarded on March 2, 2009, one-third vested on March 2, 2011, as the sole performance target was achieved in the first year of the vesting period, and the remaining two-thirds will vest in two equal annual installments beginning on March 2, 2012. Of the restricted stock units for 10,000 shares separately awarded on March 2, 2009, one-half vested on March 2, 2011, as the performance target for that installment was achieved, and one-half will vest on March 2, 2012 subject to the achievement of the remaining performance target. Of the restricted stock units for 15,000 shares awarded on May 25, 2010, one-third will vest on May 25, 2011, as the performance target for that installment was achieved, and the remaining two-thirds will vest in two equal annual installments beginning on May 25, 2012 subject to the achievement of a performance target in each year of the vesting period. The restricted stock units for 30,000 shares separately awarded on May 25, 2010 will be cancelled in May 2011 because the performance target was not achieved.

(12) The awards shown will vest in four equal annual installments beginning on May 25, 2011.

(13) Of the restricted stock units for 37,000 shares awarded on February 22, 2008, one-half vested on February 22, 2011 and one-half will vest on February 22, 2012. The restricted stock units for 7,500 shares awarded on December 9, 2009 will vest in three equal annual installments beginning on December 9, 2011.

(14) Of the awards shown, restricted stock units for 2,333 shares awarded on March 3, 2008 were cancelled in March 2011 because the performance target was not achieved. Of the restricted stock units for 10,500 shares awarded on March 2, 2009, one-third vested on March 2, 2011, as the sole performance target was satisfied in the first year of the vesting period, and the remaining two-thirds will vest in two equal annual installments beginning on March 2, 2012. Of the restricted stock units for 4,667 shares separately awarded on March 2, 2009, one-half vested on March 2, 2011, as the performance target for that installment was achieved, and one-half will vest on March 2, 2012 subject to the achievement of the remaining performance target. Of the restricted stock units for 20,000 shares awarded on March 26, 2010, one-third vested on March 26, 2011, as the performance target for that installment was achieved, and the remaining two-thirds will vest in two equal annual installments beginning on March 26, 2012 subject to the achievement of a performance target in each year of the vesting period. The restricted stock units for 40,000 shares separately awarded on March 26, 2010 were cancelled in March 2011 because the performance target was not achieved.

(15) The awards shown will vest in three equal annual installments beginning on December 9, 2011.

(16) Of the awards shown, restricted stock units for 2,333 shares awarded on March 3, 2008 were cancelled in March 2011 because the performance target was not achieved. Of the restricted stock units for 10,500 shares awarded on March 2, 2009, one-third vested on March 2, 2011, as the sole performance target was achieved in the first year of the vesting period, and the remaining two-thirds will vest in two equal annual installments beginning on March 2, 2012. Of the restricted stock units for 4,667 shares separately awarded on March 2, 2009, one-half vested on March 2, 2011, as the performance target for that installment was achieved, and one-half will vest on March 2, 2012 subject to the achievement of the remaining performance target. Of the restricted stock units for 15,000 shares awarded on March 26, 2010, one-third vested on March 26, 2011, as the performance target for that installment was achieved, and the remaining two-thirds will vest in two equal annual installments beginning on March 26, 2012, subject to the achievement of a performance target in each year of the vesting period. The restricted stock units for 30,000 shares separately awarded on March 26, 2010 were cancelled in March 2011 because the performance target was not achieved.

(17) The awards shown will vest on December 19, 2011.

(18) Of the awards shown, restricted stock units for 3,333 shares awarded on March 3, 2008 were cancelled in March 2011 because the performance target was not achieved. Of the restricted stock units for 15,000 shares awarded on March 2, 2009, one-third vested on March 2, 2011, as the sole performance target was achieved in the first year of the vesting period, and the remaining two-thirds will vest in two equal annual installments beginning on March 2, 2012. Of the restricted stock units for 6,667 shares separately awarded on March 2, 2009, one-half vested on March 2, 2011, as the performance target for that installment was achieved, and one-half will vest on March 2, 2012 subject to the achievement of the remaining performance target. Of the restricted stock units for 20,000 shares awarded on March 26, 2010, one-third vested on March 26, 2011, as the performance target for that installment was achieved, and the remaining two-thirds will vest in two equal annual installments beginning on March 26, 2012 subject to the achievement of a performance target in each year of the vesting period. The restricted stock units for 40,000 shares separately awarded on March 26, 2010 were cancelled in March 2011 because the performance target was not achieved.

(19) Of the awards shown, restricted stock units for 11,361 shares awarded on February 27, 2007 vested on February 27, 2011. The restricted stock units for 500 shares awarded on August 31, 2007 will vest on August 31, 2011. Of the restricted stock units for 8,000 shares awarded on February 22, 2008, one-half vested on February 22, 2011 and one-half will vest on February 22, 2012. The restricted stock units for 3,500 shares awarded on December 18, 2008 will vest in two equal annual installments beginning on December 18, 2011.

(20) Of the awards shown, restricted stock units for 1,333 shares awarded on March 3, 2008 were cancelled in March 2011 because the performance target was not achieved. Of the restricted stock units for 10,500 shares awarded on March 2, 2009, one-third vested on March 2, 2011, as the sole performance target was achieved in the first year of the vesting period, and the remaining two-thirds will vest in two equal annual installments beginning on March 2, 2012. Of the restricted stock units for 4,667 shares separately awarded on March 2, 2009, one-half vested on March 2, 2011, as the performance target for that installment was achieved, and one-half will vest on March 2, 2012 subject to the achievement of the remaining performance target. Of the restricted stock units for 15,000 shares awarded on March 26, 2010, one-third vested on March 26, 2011, as the performance target for that installment was achieved, and the remaining two-thirds will vest in two equal annual installments beginning on March 26, 2012 subject to the achievement of a performance target in each year of the vesting period. The restricted stock units for 30,000 shares separately awarded on March 26, 2010 were cancelled in March 2011 because the performance target was not achieved.

(21) The awards shown will vest on August 31, 2011.

(22) The awards shown will vest in two equal annual installments beginning on September 3, 2011.

(23) The awards shown will vest in two equal annual installments beginning on December 18, 2011.

Table of Contents

Option Exercises and Stock Vested

The following table presents information with respect to the options exercised and stock awards vested during 2010 for the named executive officers.

2010 Option Exercises and Stock Vested Table

	Option Awards		Stock Awards	
Name	**Number of Shares Acquired on Exercise (#)(1)**	**Value Realized on Exercise ($)(2)**	**Number of Shares Acquired on Vesting (#)(1)**	**Value Realized on Vesting ($)(3)**
Arunas A. Chesonis			25,000	105,950
Edward J. Butler, Jr.	83,680	252,593	235,990	852,855
Keith M. Wilson			203,530	737,946
Robert D. Moore, Jr.			36,888	139,726
Laurie L. Zaucha	8,000	29,760	8,166	35,581
Mario DeRiggi			53,995	202,775
Mary K. O Connell			11,416	48,261

(1) Amounts shown have not been adjusted to reflect shares sold to cover the exercise cost of the aggregate stock options exercised or the withholding of shares in payment of withholding taxes associated with stock option exercises or the vesting of restricted stock units.

(2) Dollar amounts shown are determined by multiplying (a) the number of shares of common stock subject to the options exercised by (b) the difference between the closing price of the common stock on the NASDAQ Global Select Market on the exercise date and the exercise price of the stock option.

(3) Dollar amounts shown are determined by multiplying (a) the number of shares of common stock subject to restricted stock units awards that vested by (b) the closing price of the common stock on the NASDAQ Global Select Market on the vesting date.

Termination and Change of Control Payments

Each of our named executive officers is entitled to receive payments from PAETEC under special circumstances. Generally, we will be obligated to make these payments upon a termination of the officer s employment or upon a change of control of our company.

The circumstances that would trigger these payments and the estimated amounts of the payments are set forth below. In accordance with the SEC s rules, the quantitative disclosures in this section assume that the triggering event took place on December 31, 2010, although no named executive officer s employment terminated on December 31, 2010 and no change of control of our company occurred on that date. If a triggering event were to occur in the future, actual payments could be different from the payments presented below. The employment with the company of Mr. Butler, formerly Executive Vice President and President of PAETEC s Energy Business, terminated on November 5, 2010. For further information about the actual payments Mr. Butler is entitled to receive in connection with his termination, see Actual Payment Obligations to Former Named Executive Officer below. We have omitted any discussion of potential payments to Mr. Butler based on the assumed occurrence of a triggering event on December 31, 2010 because his actual termination occurred before such date.

The market value of the restricted stock unit awards we show below is determined by multiplying the closing price of our common stock as reported on the NASDAQ Global Select Market on December 31, 2010, or $3.74 per share, by the number of shares of common stock subject to the awards. This valuation does not take into account the diminution in value attributable to the restrictions applicable to the common stock subject to restricted stock units. The market value of the stock option awards we show below is based on the difference between the value of PAETEC common stock on December 31, 2010 of $3.74 per share and the exercise price of each of the unvested options.

Table of Contents

The amounts shown in the tables below exclude, to the extent permitted under the SEC s rules, obligations due from us to the named executive officer following a triggering event for:

- any earned and vested but unpaid salary, annual incentive compensation and long-term incentive compensation through the date of termination;
- vested benefits under the employee 401(k) plan and all other benefit plans applicable to all of our employees in accordance with their terms and conditions;
- accrued vacation pay;
- reimbursement of reasonable business expenses incurred and unpaid before the date of termination; and
- any other compensation or benefits to which the named executive officer may be entitled under and in accordance with our generally applicable non-discriminatory plans or employee benefit programs.

Severance Agreements. We are required to provide some termination and change of control payments to each named executive officer under the officer s executive confidentiality, non-solicitation, non-competition and severance agreement with us entered into on February 22, 2008. The agreements for five of our named executive officers, Mr. Chesonis, Mr. Moore, Mr. DeRiggi, Ms. O Connell, and Ms. Zaucha, were revised on March 26, 2010 to reduce the amount of cash severance payable upon any voluntary termination of their employment by those officers. In addition, on January 1, 2011, Ms. O Connell entered into the form of severance agreement applicable to certain executive vice presidents of PAETEC, which superseded her prior agreement applicable to certain senior vice presidents of PAETEC. The discussion below assumes that the terms of Ms. O Connell s current agreement were in effect as of December 31, 2010.

Non-Solicitation and Non-Competition Covenants. Each severance agreement conditions the payments and other benefits described below on continued compliance by the named executive officer with two-year non-solicitation and non-competition covenants, except in the case of Ms. Zaucha, whose severance agreement contains one-year non-solicitation and non-competition covenants. The covenants provide that, for two years (or one year in the case of Ms. Zaucha) after the termination of such officer s employment for any reason, the officer will not:

- solicit, recruit or hire any of the employees or sales agents of PAETEC or any of its subsidiaries;
- serve as an officer, director, employee, 1% or greater stockholder, consultant, contractor, partner, joint venturer, agent, manager or other representative of any enterprise that is competitive with PAETEC s business or any of its subsidiaries in any geographical area in which the companies are then conducting operations, or that would divert business from PAETEC or any subsidiary in any such geographical area; or
- take any action to influence PAETEC s customers, prospective customers, vendors or suppliers or any of its subsidiaries to divert their business to a competitive enterprise, or solicit or accept business from any customer or prospective customer of PAETEC or any subsidiary on behalf of any competitive enterprise.

If an applicable final judgment is obtained that a named executive officer violated the terms of these covenants, we may, in addition to all other available remedies, discontinue the provision of the payments and benefits described below, including continued vesting of the applicable equity awards.

Severance Payments and Benefits Before Change of Control. If a named executive officer complies with the foregoing non-solicitation and non-competition covenants, the executive will be entitled to receive payment of the following amounts and benefits following termination of the executive s employment for any reason other than death, disability or, in specified circumstances, cause, as described below:

salary continuation during the applicable covenant period in an amount equal to the highest annualized base salary paid to the named executive officer at any time during the one-year period before the executive s employment was terminated, except that if the employment of Mr. Chesonis, Mr. Wilson or Ms. Zaucha is terminated by PAETEC without cause or by such named executive officer for good

Table of Contents

reason, as described below, within one year following the consummation of a change of control transaction, as described below, the executive will be entitled to receive an amount equal to 1.5 times such base salary; and

payment of elected COBRA premiums for medical and dental plan benefits during the covenant period, as well as the premiums for company-provided life insurance that the named executive officer elects to continue after the executive s employment terminates.

The named executive officers also may be entitled to an additional severance payment related to the annual bonus payment as follows:

if the employment of Mr. Chesonis, Mr. Moore, Mr. DeRiggi, Ms. O Connell or Ms. Zaucha is terminated by such named executive officer for good reason or by PAETEC without cause, such named executive officer also will be entitled to an additional severance payment for each annual bonus period ending during the applicable covenant period equal to the lesser of (1) the target bonus amount which the named executive officer would have been eligible to receive under PAETEC s annual bonus plan if the executive had been employed during the entire bonus year and the particular bonus target had been fully achieved at the target level (as opposed to the maximum level), or (2) if the amount achieved is less than the target level, the amount that is achieved (and in the event that no bonus is achieved, no amount will be paid), except that, if such named executive officer s employment is terminated by PAETEC without cause or by such named executive officer for good reason within one year following the consummation of a change of control transaction, then the foregoing clause (2) will not apply and the target level bonus will be paid; and

if the employment of Mr. Wilson is terminated for any reason other than death, disability or, in specified circumstances, cause, Mr. Wilson also will be entitled to an additional severance payment for each annual bonus period ending during the applicable covenant period equal to the target bonus amount which Mr. Wilson would have been eligible to receive under PAETEC s annual bonus plan if he had been employed during the entire bonus year.

If the named executive officer s employment is terminated for cause and PAETEC elects to waive the named executive officer s compliance with the non-solicitation and non-competition covenants, the executive will not be entitled to receive any of the foregoing severance payments and benefits.

As defined in the severance agreements, cause means the termination of the executive s employment as a result of any of the following events:

the named executive officer s material failure or refusal to perform the duties assigned to the executive, so long as the duties are not materially inconsistent with those of other individuals reporting directly to the officer of PAETEC to whom the named executive officer directly reports (or to the board of directors, in the case of the chief executive officer);

the named executive officer s refusal to follow the reasonable directives of the board of directors, the chief executive officer or the other officer to whom the named executive officer directly reports, as applicable, so long as the directives are not materially inconsistent with those applicable to other individuals reporting directly to the officer of the company to whom the named executive officer directly reports (or to the board of directors, in the case of the chief executive officer); or

the named executive officer s conviction of a felony.

Subject to specified conditions, a named executive officer will be deemed to have terminated the officer s employment for good reason as the result of any of the following events:

any action by PAETEC to reduce the responsibilities, duties or position of the executive to a materially lesser status or degree;

any action by PAETEC to reduce the executive s base salary by a material amount;

Table of Contents

any action by PAETEC to reduce the executive s target annual bonus opportunity, expressed as a percentage of the executive s annual base salary, by a material amount; or

a requirement by PAETEC that the executive be based anywhere other than within 50 miles of the executive s current location without the executive s consent.

Assuming a December 31, 2010 employment termination event unrelated to a change of control by PAETEC without cause or by the named executive officer for good reason, the aggregate payments over the two-year covenant period (or one-year covenant period in the case of Ms. Zaucha) are estimated to be as follows:

Name	Salary Due ($)	Bonus Due ($)(1)	Benefits and Health Programs ($)(2)	Total Due ($)
Arunas A. Chesonis	1,000,000	750,000	23,842	1,773,842
Keith M. Wilson	660,000	495,000	23,842	1,178,842
Robert D. Moore, Jr.	500,000	250,000	23,842	773,842
Laurie L. Zaucha	250,000	100,000	8,835	358,835
Mario DeRiggi	600,000	300,000	23,842	923,842
Mary K. O Connell	500,000	250,000	13,327	763,327

(1) Assumes named executive officer is entitled to receive the target amount payable to the executive under the annual cash bonus plan. The bonus as shown above would not be payable if the employment of Mr. Chesonis, Mr. Moore, Mr. DeRiggi, Ms. O Connell or Ms. Zaucha is not terminated by such officer for good reason or by PAETEC without cause.

(2) Assumes continuation for the covenant period of elected COBRA premiums for a family health insurance contract and premium payments based on continued life insurance for two years in the amount of base salary at the date of termination (or one year in the case of Ms. Zaucha).

Severance Payments and Benefits After Change of Control. If the employment of Mr. Chesonis, Mr. Wilson, or Ms. Zaucha is terminated by PAETEC without cause or such executive officer terminates employment for good reason within one year following a change of control transaction involving our company, PAETEC will be obligated to make payments to such named executive officer for each of the two years after termination of such executive s employment (or one year in the case of Ms. Zaucha) in an amount equal to 1.5 times the highest annualized base salary paid to such executive at any time during the one-year period immediately preceding the employment termination date. If the employment of Mr. Moore, Mr. DeRiggi or Ms. O Connell is terminated by PAETEC without cause or such executive officer terminates employment for good reason within one year following a change of control transaction involving our company, PAETEC will be obligated to make payments to such named executive officer for each of the two years after termination of the executive s employment in an amount equal to the highest annualized base salary paid to such executive at any time during the one-year period immediately preceding the employment termination date.

Each severance agreement defines change of control transaction generally to include each of the following transactions:

the dissolution or liquidation of PAETEC;

a merger or similar transaction involving PAETEC in which it is not the surviving entity or which results in PAETEC becoming a wholly-owned subsidiary of another entity, unless the stockholders of PAETEC immediately before the transaction collectively beneficially own more than 50% of the voting power of the company s successor;

a sale of all or substantially all of PAETEC s assets;

any other transaction that results in any person, other than Mr. Chesonis and his controlled affiliates, beneficially owning immediately after the transaction more than 50% of the voting power of PAETEC or a successor entity; and

Table of Contents

any event as a result of which the members of the PAETEC board of directors as of February 22, 2008, and any members subsequently appointed or nominated by a majority of the incumbent directors, cease to constitute a majority of the directors of PAETEC before the transaction or a majority of the directors of the entity whose voting securities are issued to PAETEC s stockholders in the transaction.

Assuming a December 31, 2010 termination event as described above, following a change of control transaction, the aggregate payments over the two-year covenant period to Messrs. Chesonis, Wilson, Moore and DeRiggi and Ms. O Connell, and over the one-year covenant period to Ms. Zaucha, are estimated to be as follows:

Name	**Salary Due ($)**	**Bonus Due ($)(1)**	**Benefits and Health Programs ($)(2)**	**Total Due ($)**
Arunas A. Chesonis	1,500,000	750,000	23,842	2,273,842
Keith M. Wilson	990,000	495,000	23,842	1,508,842
Robert D. Moore, Jr.	500,000	250,000	23,842	773,842
Laurie L. Zaucha	375,000	100,000	8,835	483,835
Mario DeRiggi	600,000	300,000	23,842	923,842
Mary K. O Connell	500,000	250,000	13,327	763,327

(1) Assumes the named executive officer is entitled to receive the target amount payable to the executive under the annual cash bonus plan.

(2) Assumes continuation for the covenant period of elected COBRA premiums for a family health insurance contract and premium payments based on continued life insurance for two years in the amount of base salary at the date of termination (or one year in the case of Ms. Zaucha).

Terms of All Payments. The salary continuation payments will be made in installments during the covenant period in accordance with PAETEC s customary payroll practices, while the payments equal to the annual bonus amounts will be made in accordance with PAETEC s annual bonus payout practices.

PAETEC may elect to discontinue the payments and provision of other severance benefits described above if:

it determines in good faith that the executive has violated the terms of any of the foregoing non-solicitation and non-competition covenants; or

a court determines in an action initiated by the executive that any of the foregoing covenants is void or unenforceable.

Continued and Accelerated Vesting of Equity-Based Awards Made After February 21, 2008. Each severance agreement provides that equity-based awards made to the named executive officer on or after February 22, 2008 will include provisions to the following effect:

the awards will continue to vest over the covenant period after the termination of the executive s employment by PAETEC without cause or by the executive for good reason;

immediately before the consummation of a change of control transaction, all restricted stock, restricted stock unit and similar awards will vest and the shares subject to the awards will be delivered to the executive; and

15 days before the scheduled consummation of a change of control transaction, all stock options, stock appreciation rights and similar awards will become exercisable and will remain exercisable until the transaction is consummated.

Continued and Accelerated Vesting of Equity Awards Outstanding as of December 31, 2010. As of December 31, 2010, the named executive officers had, as specified below, unvested restricted stock units and

unvested stock options that were entitled to continued vesting or accelerated vesting upon specified events of change of control or upon the termination of the named executive officer s employment in some circumstances under provisions of the severance agreements described above and of the incentive plans and award agreements under which the awards were granted.

The senior officer confidentiality, non-solicitation, non-competition and severance agreements that were in effect between PAETEC and each named executive officer before February 22, 2008, which we refer to as the prior severance agreements, provided that unvested stock options and restricted stock units would continue to vest after the termination of employment under specified circumstances during the non-solicitation and non-competition covenant periods under those agreements. The new severance agreements entered into after such time generally preserve the terms and conditions of vesting of awards outstanding at the time the severance agreements were entered into, except that continued vesting is now subject to compliance with the non-solicitation and non-competition covenants contained in such agreements.

Our named executive officers hold unvested equity awards granted under the PAETEC Holding Corp. 2007 Omnibus Incentive Plan, which we refer to as the 2007 omnibus incentive plan. As described in more detail below, the 2007 omnibus incentive plan and the award agreements under the 2007 omnibus incentive plan provide for accelerated vesting of unvested options and restricted stock units in some circumstances, and continued vesting of the awards after termination of employment in other circumstances, subject to compliance with the non-solicitation and non-competition covenants contained in the severance agreements.

We describe below the effects which the various triggering events would have had on the vesting of these outstanding awards held by our named executive officers if the events had occurred as of December 31, 2010.

Stock Options. As of December 31, 2010, each of the named executive officers holds unvested stock options awarded under the 2007 omnibus incentive plan. These stock option awards are subject to the terms of the executive s severance agreements. For further information about these stock options, see the 2010 Outstanding Equity Awards at Fiscal Year-End Table above. Under the terms of the applicable option award agreements, these stock options will continue to vest following termination of the executive s employment by PAETEC without cause or by the executive for good reason, as defined in the severance agreements, during the two-year covenant period under the severance agreements for Messrs. Chesonis, Wilson, Moore and DeRiggi and Ms. O Connell, and during the one-year covenant period under the severance agreement for Ms. Zaucha. PAETEC may discontinue vesting if it obtains a qualified judicial determination that the covenants were violated. The award agreements also provide that 15 days before the scheduled consummation of a change of control transaction, as defined in the severance agreements, all stock options will become exercisable and will remain exercisable until the transaction is consummated.

In the event of the named executive officer s death or disability, no acceleration of vesting or continued vesting will apply to stock options granted to the executive under the 2007 omnibus incentive plan.

Table of Contents

Assuming the occurrence on December 31, 2010 of a covered termination of the named executive officers or a covered change of control, the number and value of stock options that would have been entitled to continued or accelerated vesting under the 2007 omnibus incentive plan are set forth below. The value of the stock options is calculated based on the difference between the value of PAETEC common stock on December 31, 2010 of $3.74 per share, which was the closing sale price of the common stock on that date as reported on the NASDAQ Global Select Market, and the exercise price of each of the unvested options that would be subject to continued or accelerated vesting. The actual value on the vesting date of the stock options subject to continued vesting will depend on the value of PAETEC s common stock on that date.

	Termination Without Cause or For Good Reason Continued Vesting		Change of Control Accelerated Vesting	
Name	**Number of Stock Options (#)**	**Value of Stock Options ($)**	**Number of Stock Options (#)**	**Value of Stock Options ($)**
Arunas A. Chesonis	40,000	18,450	68,750	27,675
Keith M. Wilson	22,500	18,450	33,750	27,675
Robert D. Moore, Jr.	22,000	8,610	36,250	12,915
Laurie L. Zaucha	19,750	19,680	48,750	59,040
Mario DeRiggi	20,000	12,300	32,500	18,450
Mary K. O Connell	21,500	25,975	32,500	34,585

Restricted Stock Units. As of December 31, 2010, all of the named executive officers held unvested restricted stock units awarded under the 2007 omnibus incentive plan. The restricted stock units are subject to the terms of the executive s severance agreements. For additional information about these restricted stock units, see the 2010 Outstanding Equity Awards at Fiscal Year-End Table above. Under the terms of the applicable option award agreements, these restricted stock units will continue to vest following termination of employment by PAETEC without cause or by the executive for good reason, as defined in the severance agreements, during the two-year covenant period under the severance agreements for Messrs. Chesonis, Wilson, Moore and DeRiggi and Ms. O Connell, and over the one-year covenant period under the severance agreement for Ms. Zaucha. PAETEC may discontinue vesting if it obtains a qualified judicial determination that the covenants were violated. The award agreements also provide that all restricted stock units will vest immediately before the consummation of a change of control transaction, as defined in the severance agreements, as well as upon the executive s death or disability.

Assuming the occurrence on December 31, 2010 of a covered termination of the named executive officers, a change of control, or any other triggering event as described above, the number and value of restricted stock units that would have been entitled to continued or accelerated vesting for each named executive officer under the 2007 omnibus incentive plan are as set forth below. The value of the restricted stock units is calculated based on the value of PAETEC common stock on December 31, 2010 of $3.74 per share, which was the closing sale price of the common stock on that date as reported on the NASDAQ Global Select Market. The actual value on the vesting date of the restricted stock units subject to continued vesting will depend on the value of PAETEC s common stock on that date.

	Termination Without Cause or For Good Reason Continued Vesting		Change of Control/ Death or Disability Accelerated Vesting	
Name	**Number of RSUs (#)**	**Value of RSUs ($)**	**Number of RSUs (#)**	**Value of RSUs ($)**
Arunas A. Chesonis	228,333	853,965	302,500	1,131,350
Keith M. Wilson	150,000	561,000	177,500	663,850
Robert D. Moore, Jr.	89,334	334,109	122,001	456,284
Laurie L. Zaucha	35,667	133,395	92,501	345,954
Mario DeRiggi	103,334	386,469	135,001	504,904
Mary K. O Connell	61,362	229,494	84,862	317,384

Table of Contents

Actual Payment Obligations to Former Named Executive Officer. Effective on November 5, 2010, Mr. Butler s employment as Executive Vice President and President of PAETEC s Energy Business was terminated. As a result of his termination, Mr. Butler is entitled to receive the termination payments described below pursuant to his severance agreement.

Mr. Butler is entitled to receive, during each of the two years following his termination, an amount equal to his highest annualized base salary paid to him at any time during the one-year period preceding his resignation. This amount is payable in accordance with the company s normal payroll practices beginning in May 2011. Mr. Butler also is entitled to receive in May 2011 and March 2012 payments in an amount approximately equal to the target bonus opportunity for each of 2010 and 2011, respectively, that he would have been eligible to receive under PAETEC s annual bonus plan and his severance agreement. Mr. Butler is also entitled to receive benefits continuation coverage as described in his severance agreement, including elected COBRA premiums for a family health insurance contract and premium payments based on continued life insurance for two years in the amount of Mr. Butler s base salary at the date of termination. Payment of these amounts and benefits is conditioned upon continued compliance with the non-solicitation and non-competition covenants in Mr. Butler s severance agreement.

Under the terms of equity-based award agreements between Mr. Butler and the company, Mr. Butler is entitled to the continued vesting of options to purchase 22,500 shares of PAETEC common stock and of restricted stock units for 150,000 shares of PAETEC common stock. The continued vesting also is conditioned upon continued compliance with the non-solicitation and non-competition covenants in Mr. Butler s severance agreement.

The following table sets forth the payments Mr. Butler is entitled to receive in connection with the termination of his employment:

Payments Upon Termination	**Value ($)**
Cash Compensation and Benefits:	
Salary continuation under severance agreement	660,000
Payment in lieu of bonuses	495,000
Benefits continuation	23,842
Long-Term Incentives:	
Stock options	24,375(1)
Restricted stock units	630,000(2)

(1) The value of the stock options is calculated based on the difference between the value of PAETEC s common stock on November 5, 2010, the effective date of Mr. Butler s termination, of $4.20 per share, which was the closing sale price of the common stock on that date as reported on the NASDAQ Global Select Market, and the exercise price of each unvested option that is subject to continued vesting. The actual value on the vesting date of the stock options subject to continued vesting will depend on the value of PAETEC s common stock on that date.

(2) The value of the restricted stock units is calculated based on the value of PAETEC s common stock on November 5, 2010, the effective date of Mr. Butler s termination, of $4.20 per share, which was the closing sale price of the common stock on that date as reported on the NASDAQ Global Select Market. The actual value on the vesting date of the restricted stock units subject to continued vesting will depend on the value of PAETEC s common stock on that date.

Transactions with Related Persons

Under its charter, the PAETEC audit committee has the responsibility to conduct an appropriate review of and to approve transactions that are subject to disclosure under Item 404(a) of the SEC s Regulation S-K. Such transactions generally include those in which PAETEC or a subsidiary is a participant and in which the amount involved exceeds $120,000 in any fiscal year, if any of PAETEC s directors, director nominees, executive officers, or 5% stockholders, or an immediate family member or person sharing the household of the foregoing persons, has a direct or indirect material interest in any such transaction. We refer to all such persons as related persons. Transactions involving director and executive compensation are subject to oversight and, in some cases, approval by the compensation committee under its charter. All transactions during 2008, 2009 and 2010 that were subject to audit committee approval were reviewed and approved by the audit committee.

The following is a summary of transactions during 2008, 2009, 2010 and the first quarter of 2011 among PAETEC and its subsidiaries and the related persons identified below.

PAETEC employs as an executive officer Algimantas Chesonis, who is a brother of Arunas Chesonis, the company s Chairman, President and Chief Executive Officer. PAETEC made total salary and bonus payments to this family member of $229,703 for 2008, $200,000 for 2009, $313,676 for 2010 and $48,462 for the first quarter of 2011. PAETEC issued this family member options to purchase 7,000 shares of common stock at an exercise price of $7.64 per share and restricted stock units for 65,000 shares of common stock during 2008, options to purchase 7,000 shares of common stock at an exercise price of $1.28 per share and restricted stock units for 21,000 shares of common stock during 2009, and options to purchase 15,000 shares of common stock at an exercise price of $4.59 per share and restricted stock units for 45,000 shares of common stock during 2010.

In 2008, PAETEC entered into arrangements with an unrelated aircraft charter corporation pursuant to which it commits over a specified period to charter a minimum number of hours of flight time on the charter corporation s managed fleet of jet aircraft. One of the several jet aircraft in the charter corporation s fleet that were used by PAETEC during 2008, 2009 and 2010 is owned by a limited liability company that is 50% owned by Arunas Chesonis, PAETEC s Chairman, President and Chief Executive Officer, and 50% owned by Richard Aab, PAETEC s Vice Chairman. Under an agreement between the charter corporation and the limited liability company, the charter corporation leases the limited liability company s jet on an exclusive basis, manages the operation of the jet and solicits charter customers to use the jet. Under the agreement, the charter corporation is required to pay the limited liability company a specified rate for each flight hour for which the limited liability company s aircraft is used by customers of the charter corporation for charter services. The charter corporation also pays all associated fuel costs and other specified expenses. As a result of PAETEC s purchase of flight time from the charter corporation for use of the jet owned by the limited liability company, the charter corporation made payments to the limited liability company of $464,889 during 2008, $416,716 during 2009 and $420,674 during 2010.

During 2009, PAETEC recognized approximately $0.8 million of stock-based compensation expense in connection with an amendment to an outstanding common stock warrant held by Richard Aab, PAETEC s Vice Chairman, in order to extend the expiration date of the warrant. The warrant was originally assumed by PAETEC pursuant to the US LEC merger on February 28, 2007, at which time it was fully vested.

Table of Contents

SECURITY OWNERSHIP

The following table presents information regarding the beneficial ownership of PAETEC common stock as of April 1, 2011 by:

- each of PAETEC s directors;
- each director nominee;
- PAETEC s Chief Executive Officer, its Chief Financial Officer and the other executive officers named in the Summary Compensation Table under Executive Compensation ;
- all directors and executive officers of PAETEC as a group; and
- each person known by PAETEC to own beneficially more than 5% of PAETEC s common stock.

The following information has been presented in accordance with the SEC s rules and is not necessarily indicative of beneficial ownership for any other purpose. Under the SEC s rules, beneficial ownership of a class of capital stock as of any date includes any shares of that class as to which a person, directly or indirectly, has or shares voting power or investment power as of that date and also any shares as to which a person has the right to acquire sole or shared voting or investment power as of or within 60 days after that date through the exercise of any stock option, warrant or other right, without regard to whether the right expires before the end of the 60-day period or continues thereafter. If two or more persons share voting power or investment power with respect to specific securities, all of those persons may be deemed to be the beneficial owners of the securities. Information with respect to persons other than the holders listed in the table below that share beneficial ownership with respect to the securities shown is set forth following the table.

As of April 1, 2011, there were 144,842,543 shares of PAETEC common stock outstanding.

Name of Beneficial Owner	Amount and Nature of Beneficial Ownership	Percent of Class (%)
Executive Officers, Directors and Director Nominees:		
Richard T. Aab	8,391,543	5.8
Edward J. Butler, Jr.	1,121,894	*
Arunas A. Chesonis	7,589,191	5.2
Mario DeRiggi	323,710	*
Shelley Diamond	50,498	*
H. Russell Frisby, Jr.	144,057	*
Tansukh V. Ganatra	2,421,761	1.7
Michael C. Mac Donald	100,998	*
William R. McDermott	104,857	*
Robert D. Moore, Jr.	316,103	*
Mary K. O Connell	69,689	*
Alex Stadler	139,798	*
Keith M. Wilson	1,430,559	1.0
Laurie Zaucha	56,739	*
Mark Zupan	176,723	*
All directors and executive officers as a group (16 persons)	22,687,353	15.4
Other Stockholders:		
BlackRock, Inc.	8,871,966	6.1

Columbia Wanger Asset Management, L.P.	14,743,000	10.2
FMR LLC	8,024,360	5.5
Penn Capital Management	7,921,094	5.5
Sankaty Credit Opportunities III, L.P. and others	7,801,908	5.4
Wayzata Investment Partners LLC	12,876,887	8.9

* Represents beneficial ownership of less than 1%.

Table of Contents

The percentage of beneficial ownership as to any person as of a particular date is calculated by dividing the number of shares beneficially owned by the person, which includes the number of shares as to which the person has the right to acquire voting or investment power as of or within 60 days after such date, by the sum of the number of shares outstanding as of the date plus the number of shares as to which the person has the right to acquire voting or investment power as of or within 60 days after such date. Consequently, the denominator for calculating beneficial ownership percentages may be different for each beneficial owner.

The information concerning Mr. Aab is based on PAETEC s records and on information filed with the SEC on Schedule 13D/A on December 17, 2009. Mr. Aab reports that the shares of common stock shown as beneficially owned by him include shares held by Melrich Associates, L.P., for which Mr. Aab and his wife are the sole general partners and share voting and investment power. The amount shown in the table also includes 811,639 shares issuable upon the exercise of stock options and warrants that are exercisable as of or within 60 days after April 1, 2011. Mr. Aab s address is c/o PAETEC Holding Corp., One PAETEC Plaza, 600 Willowbrook Office Park, Fairport, New York 14450.

The shares of common stock shown as beneficially owned by Mr. Butler are based on PAETEC s records as of the termination of Mr. Butler s employment on November 5, 2010 and include 11,250 shares issuable upon the exercise of stock options that were exercisable as of or within 60 days after such date.

The information concerning Mr. Chesonis is based on PAETEC s records and on information filed with the SEC on Schedule 13D/A on May 17, 2010. The shares of common stock shown as beneficially owned by Mr. Chesonis include 548,535 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011. Mr. Chesonis s address is c/o PAETEC Holding Corp., One PAETEC Plaza, 600 Willowbrook Office Park, Fairport, New York 14450.

The shares of common stock shown as beneficially owned by Mr. DeRiggi include 52,232 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by Ms. Diamond include 44,332 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by Mr. Frisby include 132,891 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by Mr. Ganatra include 342,500 shares as to which Mr. Ganatra has sole voting and investment power through a stock control agreement with his son, 235,000 shares as to which Mr. Ganatra has sole voting and investment power through a stock control agreement with his wife, 1,700,000 shares held in charitable remainder trusts for which Mr. Ganatra has sole voting and investment power, and 19,499 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by Mr. Mac Donald include 15,832 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by Mr. McDermott include 52,598 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by Mr. Moore include 87,656 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by Ms. O Connell include 42,611 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

Table of Contents

The shares of common stock shown as beneficially owned by Mr. Stadler include 130,632 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by Mr. Wilson include 707,898 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by Ms. Zaucha are based on PAETEC s records as of the termination of Ms. Zaucha s employment on March 4, 2011 and include 48,250 shares issuable upon the exercise of stock options that were exercisable as of or within 60 days after such date.

The shares of common stock shown as beneficially owned by Mr. Zupan include 149,224 shares issuable upon the exercise of stock options that are exercisable as of or within 60 days after April 1, 2011.

The shares of common stock shown as beneficially owned by all directors and executive officers as a group include 2,942,487 shares issuable upon the exercise of stock options and warrants that are exercisable as of or within 60 days after April 1, 2011, or, with respect to the executive officers identified above who are no longer employed by PAETEC, as of or within the dates indicated above.

The information concerning BlackRock, Inc. is based on information filed with the SEC on Schedule 13G on February 7, 2011. BlackRock, Inc. reports sole dispositive and sole voting power over all of the shares shown. BlackRock, Inc. s address is 40 East 52nd Street, New York, New York 10022.

The information concerning Columbia Wanger Asset Management, L.P. is based on information filed with the SEC on Schedule 13G/A on February 11, 2011. Columbia Wanger Asset Management, L.P. reports that it has sole dispositive power over all of the shares shown and sole voting power over 13,518,000 of the shares shown. The shares shown include shares held by Columbia Acorn Trust, a Massachusetts business trust advised by the reporting person. Columbia Wanger Asset Management, L.P. s address is 227 West Monroe Street, Suite 3000, Chicago, Illinois 60606.

The information concerning FMR LLC, or FMR, is based on information filed with the SEC on Schedule 13G/A on February 14, 2011. FMR reports that the shares of common stock shown as beneficially owned by it include 7,624,220 shares beneficially owned by Fidelity Management & Research Company, or Fidelity, a wholly-owned subsidiary of FMR and an investment adviser registered under Section 203 of the Investment Advisers Act of 1940, as a result of Fidelity s service as investment adviser to various investment companies. Each of Edward C. Johnson, III, the Chairman of FMR, FMR, through its control of Fidelity, and unnamed investment companies has sole power to dispose of the shares owned by the investment companies. Members of the family of Mr. Johnson are the predominant owners of FMR and may be deemed, under the Investment Company Act of 1940, to form a controlling group with respect to FMR. Neither FMR nor Mr. Johnson has the sole power to vote or direct the voting of the shares owned directly by any investment company, which power resides with each such investment company s board of trustees. Pyramis Global Advisors Trust Company, an indirect, wholly-owned subsidiary of FMR and a bank, is the beneficial owner of 400,140 shares of common stock as a result of its serving as investment manager of institutional accounts owning such shares. Mr. Johnson and FMR each has sole dispositive power over 400,140 shares of common stock and sole power to vote or direct the voting of 400,140 shares of common stock owned by the institutional accounts managed by Pyramis Global Advisors Trust Company. FMR s address is 82 Devonshire Street, Boston, Massachusetts 02109.

The information concerning Penn Capital Management is based on information filed with the SEC on Schedule 13G on February 15, 2011. Penn Capital Management reports sole voting and dispositive power over all of the shares shown. Penn Capital Management s address is Navy Yard Corporate Center, Three Crescent Drive, Suite 400, Philadelphia, Pennsylvania 19112.

The information concerning Sankaty Credit Opportunities III, L.P. and others is based on information filed with the SEC on Schedule 13G on February 14, 2011 by Sankaty Credit Opportunities III, L.P., or COPS III, Sankaty Credit Opportunities IV, L.P., or COPS IV, Sankaty Credit Opportunities (Offshore) IV, L.P., or COPS IV Offshore, and Sankaty Advisors, LLC in its capacity as the investment manager for a managed account client. The Schedule 13G states that COPS III has sole voting and dispositive power with respect to 2,425,677 shares of common stock, COPS IV has sole voting and dispositive power with respect to 2,046,296 shares of common stock, COPS IV Offshore has sole voting and dispositive power with respect to 2,636,310 shares of common stock, and Sankaty Advisors, LLC has sole voting and dispositive power with respect to 693,625 shares of common stock. The reporting persons also state that Sankaty Credit Member, LLC is the managing member of COPS III and COPS IV, that Sankaty Credit Member (Offshore), Ltd. is the general partner of COPS IV Offshore, that Sankaty Advisors, LLC has entered into an investment management agreement with a managed account client pursuant to which it has authority to acquire, dispose of, and vote securities on behalf of such client, and that Jonathan S. Lavine is the managing member of Sankaty Credit Member, LLC and a director of Sankaty Credit Member (Offshore), Ltd. The address for COPS III, COPS IV, COPS IV Offshore and Sankaty Advisors, LLC is 111 Huntington Avenue, Boston, Massachusetts 02199.

The information concerning Wayzata Investment Partners LLC, or Wayzata, is based on information filed with the SEC on Schedule 13G/A on February 14, 2011. Wayzata serves as an investment adviser to Wayzata Recovery Fund, LLC, Wayland Distressed Opportunities Fund I-B, LLC, Wayland Distressed Opportunities Fund I-C, LLC, Wayzata Opportunities Fund II, L.P., Wayzata Opportunities Fund Offshore II, L.P., Wayzata Opportunities Fund, LLC, and Wayzata Opportunities Fund Offshore, L.P. Wayzata and Patrick J. Halloran, an individual who serves as the managing member of Wayzata, report that they share voting and dispositive power over all of the shares shown. Wayzata and Mr. Halloran disclaim beneficial ownership of the shares owned by the funds which they manage. The address for Wayzata and Mr. Halloran is 701 East Lake Street, Suite 300, Wayzata, Minnesota 55391.

Table of Contents

DESCRIPTION OF CERTAIN INDEBTEDNESS

The following summarizes the principal terms of our indebtedness as of March 31, 2011.

Senior Secured Credit Facilities

As of March 31, 2011, our senior secured credit facilities consisted of the following:

- a term loan credit facility under which no term loans are outstanding and under which we may obtain incremental term loans, subject to conditions, in an aggregate principal amount of up to approximately $65 million under one or more incremental facilities; and

- a revolving credit facility under which we may obtain from time to time revolving loans of up to an aggregate principal amount of $50 million outstanding at any time, of which $25.0 million principal amount of revolving loans are outstanding.

PAETEC Holding is the borrower under our term loan and revolving credit facilities. All obligations under the facilities are or will be guaranteed by all of PAETEC Holding s directly and indirectly owned domestic subsidiaries. The obligations of the PAETEC loan parties under the facilities are secured by first-priority liens on, and first-priority security interests in, substantially all of their assets.

The PAETEC loan parties may elect, subject to pro forma compliance with a total leverage ratio covenant and other conditions, to solicit the lenders under the credit facility agreement or other prospective lenders to extend up to $65 million total principal amount of term loans under one or more incremental term loan facilities. The maximum aggregate principal amount of incremental term loan facilities we may obtain will be reduced by the total principal amount of any senior secured notes that we may issue in the future. Borrowings under any such incremental term loan facility may be used for working capital, capital expenditures and general corporate purposes. The indenture that will govern the exchange notes limits our ability to obtain borrowings under our senior secured credit facilities. For additional information, see Description of the Exchange Notes Certain Covenants Limitation on Indebtedness.

We may use the proceeds of loans under the revolving credit facility for working capital, capital expenditures and general corporate purposes. A portion of this facility is available for the issuance of letters of credit to support our operating requirements.

The final maturity date is February 28, 2012 for the revolving credit facility. The final maturity date for any incremental term loan facility will be fixed in the applicable incremental term loan facility commitment agreement.

There are no scheduled principal payments under the revolving loans. Any outstanding revolving loans will be payable in full on the revolving loan maturity date.

To the extent that we obtain loans under any future incremental term loan facility, we may be required to make scheduled principal payments under that facility. In addition, we may be required to make principal repayments under an incremental term loan facility from specified excess cash flows from operations and from the net proceeds of specified types of asset sales, debt issuances, and insurance recovery and condemnation events.

Interest accrued on borrowings outstanding under any incremental term loan facility generally will be payable by us on a quarterly basis. Such borrowings will bear interest, at our option, at an annual rate equal to either a specified base rate plus a margin, or LIBOR plus a margin. The margin applicable to loans under the revolving credit facility is subject to specified reductions based on certain reductions in our total leverage ratio. The base rate is equal to a specified prime lending rate or, if higher, the overnight federal funds rate plus 0.50%. Subject to availability and other conditions, we have the right to select interest periods of 1, 2, 3, 6 or, in the case of revolving credit facility borrowings (subject to the approval of revolving credit lenders), 9 or 12 months for LIBOR loans.

Table of Contents

The credit facility agreement contains customary representations and warranties by the PAETEC loan parties, as well as customary events of default. The senior secured credit facilities require the PAETEC loan parties to comply with affirmative and negative covenants customarily applicable to senior secured credit facilities, including covenants restricting the ability of the PAETEC loan parties, subject to specified exceptions, to incur additional indebtedness and additional liens on their assets, engage in mergers or acquisitions or dispose of assets, pay dividends or make other distributions, voluntarily prepay other indebtedness (including prepayments of the 9.5% senior notes, the 8 $^{7}/8$% senior secured notes and the notes), enter into transactions with affiliated persons, make investments, change the nature of their businesses and amend the terms of certain other indebtedness (including the 9.5% senior notes, the 8 $^{7}/8$% senior secured notes and the notes). The credit facility agreement permits the incurrence of $35 million of non-recourse debt to acquire our headquarters.

We are required to satisfy a total net leverage ratio under which our ratio of consolidated debt to adjusted consolidated EBITDA (as defined for purposes of the credit facility agreement) as of any measurement date will not be permitted to be greater than 5.00:1.00.

8 $^{7}/8$% Senior Secured Notes

As of March 31, 2011, we had outstanding $650 million principal amount of 8 $^{7}/8$% Senior Secured Notes due 2017, which we refer to as the 8 $^{7}/8$% senior secured notes in this prospectus.

The 8 $^{7}/8$% senior secured notes accrue interest at a rate of 8 $^{7}/8$% per year. Interest is payable semi-annually in arrears on June 30 and December 31 of each year. The 8 $^{7}/8$% senior secured notes will mature on June 30, 2017.

We may redeem some or all of the 8 $^{7}/8$% senior secured notes, at any time before June 30, 2013, at a redemption price equal to 100% of their principal amount plus a make-whole premium. We may redeem some or all of the 8 $^{7}/8$% senior secured notes, at any time on or after June 30, 2013, at specified redemption prices declining to 100% of their principal amount. In addition, before June 30, 2012, we may redeem up to 35% of the aggregate principal amount of the 8 $^{7}/8$% senior secured notes at a redemption price of 108.875% of their principal amount with the net cash proceeds of certain equity offerings. If we undergo certain kinds of changes of control, or sell certain of our assets and do not apply the net proceeds to repay indebtedness under our senior secured credit facilities or reinvest such net proceeds in our business, we may be required to offer to repurchase the 8 $^{7}/8$% senior secured notes.

The 8 $^{7}/8$% senior secured notes are PAETEC Holding s senior obligations and rank or will rank equally in right of payment with all of PAETEC Holding s existing and future senior indebtedness, including our indebtedness under our existing senior credit facilities and the exchange notes, but the exchange notes will be effectively subordinated to the 8 $^{7}/8$% senior secured notes and our existing senior credit facilities to the extent of the value of the collateral that secures such indebtedness. Our domestic restricted subsidiaries that are eligible and required under the 8 $^{7}/8$% senior secured notes indenture to do so have, jointly and severally, fully and unconditionally guaranteed, to each holder of the 8 $^{7}/8$% senior secured notes, the full and prompt performance of PAETEC Holding s obligations under the 8 $^{7}/8$% senior secured notes indenture and the 8 $^{7}/8$% senior secured notes, including the payment of principal (and premium, if any) and interest on the 8 $^{7}/8$% senior secured notes, on an equal and ratable basis. Each guarantee ranks or will rank equally in right of payment with all existing and future senior secured indebtedness of the subsidiary guarantors, including their guarantees of our existing senior secured credit facilities and the exchange notes, but their guarantees of the exchange notes will be effectively subordinated to their guarantees of the 8 $^{7}/8$% senior secured notes and our existing senior credit facilities to the extent of the value of the collateral that secures such guarantees. The 8 $^{7}/8$% senior secured notes and the related subsidiary guarantees are secured on a first-priority basis, equally and ratably with our senior secured credit facilities and any future *pari passu* secured obligations subject to permitted liens, by substantially all of our assets.

Table of Contents

The 8 $^{7}/8$% senior secured notes indenture contains covenants that, among other things, limit our ability, and the ability of our restricted subsidiaries, to incur additional indebtedness, pay dividends on, redeem or repurchase our capital stock, make investments or repay subordinated indebtedness, engage in sale-leaseback transactions, enter into transactions with affiliates, sell assets, create liens, create restrictions on dividend and other payments from our subsidiaries, issue or sell stock of subsidiaries, and engage in a merger, sale or consolidation. All of the covenants are subject to a number of important qualifications and exceptions.

9.5% Senior Notes

As of March 31, 2011, we had outstanding $300 million principal amount of 9.5% Senior Notes due 2015, which we refer to as the 9.5% senior notes in this prospectus.

The 9.5% senior notes accrue interest at a rate of 9.5% per year. Interest is payable semi-annually in arrears on January 15 and July 15 of each year. The 9.5% senior notes will mature on July 15, 2015.

We may redeem some or all of the 9.5% senior notes, at any time before July 15, 2011, at a redemption price equal to 100% of their principal amount plus a make-whole premium. We may redeem some or all of the 9.5% senior notes, at any time on or after July 15, 2011, at specified redemption prices declining to 100% of their principal amount. If we undergo certain kinds of changes of control, or sell certain of our assets and do not apply the net proceeds to repay indebtedness under our senior secured credit facilities or reinvest such net proceeds in our business, we may be required to offer to repurchase the 9.5% senior notes.

The 9.5% senior notes are PAETEC Holding s senior unsecured obligations and rank or will rank equally in right of payment with all of PAETEC Holding s existing and future senior indebtedness, including the exchange notes. Our domestic restricted subsidiaries that are eligible and required under the 9.5% senior notes indenture to do so have, jointly and severally, fully and unconditionally guaranteed, to each holder of the 9.5% senior notes, the full and prompt performance of PAETEC Holding s obligations under the 9.5% senior notes indenture and the 9.5% senior notes, including the payment of principal (and premium, if any) and interest on the 9.5% senior notes, on an equal and ratable basis. Each guarantee ranks or will rank equally in right of payment with all existing and future senior unsecured indebtedness of the subsidiary guarantors. The 9.5% senior notes and the guarantees are or will be effectively subordinated in right of payment to all of the existing and future secured obligations of PAETEC Holding and the subsidiary guarantors, including our senior secured credit facilities, the 8 $^{7}/8$% senior secured notes and the guarantees of all such indebtedness, to the extent of the value of the assets securing those obligations.

The 9.5% senior notes indenture contains covenants that, among other things, limit our ability, and the ability of our restricted subsidiaries, to incur additional indebtedness, pay dividends on, redeem or repurchase our capital stock, make investments or repay subordinated indebtedness, engage in sale-leaseback transactions, enter into transactions with affiliates, sell assets, create liens, create restrictions on dividend and other payments from our subsidiaries, issue or sell stock of subsidiaries, and engage in a merger, sale or consolidation. All of the covenants are subject to a number of important qualifications and exceptions.

Other Indebtedness

Our other indebtedness as of March 31, 2011 totaled approximately $44.6 million and did not include any debt for borrowed money. For additional information regarding our indebtedness as of March 31, 2011, see Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources.

DESCRIPTION OF THE EXCHANGE NOTES

The terms of the exchange notes offered in exchange for the original notes will be substantially identical to the terms of the original notes, except that the exchange notes are registered under the Securities Act and the transfer restrictions, registration rights and related additional interest terms applicable to the original notes (as described under The Exchange Offer Purpose of the Exchange Offer Registration Rights Agreement) will not apply to the exchange notes. As a result, we refer to the original notes and the exchange notes collectively as Notes for purposes of the following summary.

From and after the consummation of the Assumption on December 6, 2010 described below under Issuance and Assumption of Original Notes, the references to the Company in the following summary refer only to PAETEC Holding Corp. and not to any of its Subsidiaries.

The following summary of certain provisions of the Indenture and the Registration Rights Agreement does not purport to be complete and is subject to, and is qualified in its entirety by reference to, all the provisions of the Indenture and the Registration Rights Agreement, including the definitions of certain terms in the Indenture, which provisions are made a part of the Indenture by reference to the Trust Indenture Act. Copies of the Indenture and the Registration Rights Agreement are available upon request from the Company. Whenever particular defined terms of the Indenture not otherwise defined herein are referred to, such defined terms are incorporated herein by reference. For definitions of certain capitalized terms used in the following summary, see Certain Definitions.

Issuance and Assumption of Original Notes

On December 2, 2010, PAETEC Escrow Corporation (the Escrow Issuer), a wholly-owned subsidiary of PAETEC Holding, issued and sold $450 million aggregate principal amount of 9 $^{7}/8$% Senior Notes due 2018 (the original notes) pursuant to an Indenture, dated as of December 2, 2010 (as amended or supplemented from time to time, the Indenture), among the Escrow Issuer and The Bank of New York Mellon Trust Company, N.A., as trustee (the Trustee). On December 2, 2010, the gross proceeds of approximately $435 million received from the offering of the original notes, together with certain additional amounts, were deposited into a segregated escrow account. On December 6, 2010, upon the effectiveness of PAETEC Holding s acquisition by merger of Cavalier and the satisfaction of other conditions, (1) PAETEC Holding assumed the Escrow Issuer s obligations and agreements in respect of the original notes and under the Indenture and (2) the escrow arrangements were terminated and the offering proceeds and other amounts were disbursed from the escrow account and used, together with cash on hand of PAETEC Holding and Cavalier, to pay the merger consideration and other costs and expenses related to the acquisition of Cavalier.

In connection with such Assumption and related transactions, PAETEC Holding and certain of its subsidiaries entered into the following agreements relating to the original notes and the Indenture effective on December 6, 2010:

First Supplemental Indenture, dated as of December 6, 2010, among the Escrow Issuer, PAETEC Holding and the Trustee, pursuant to which (1) PAETEC Holding assumed unconditionally all of the Escrow Issuer s obligations and agreements in respect of the original notes and under the Indenture on the terms and subject to the conditions set forth in of the Indenture, became bound by all other applicable provisions of the Indenture and the original notes, and agreed to perform all of the obligations and agreements of the Escrow Issuer in respect of the original notes and under the Indenture, and (2) the Escrow Issuer was unconditionally and irrevocably released and discharged from all obligations, agreements and liabilities as issuer of the original notes in respect of the original notes and under the Indenture.

Second Supplemental Indenture, dated as of December 6, 2010, among PAETEC Holding, the Escrow Issuer and the other initial Subsidiary Guarantors named therein and the Trustee, pursuant to which the eligible domestic subsidiaries of PAETEC Holding were added as parties to the Indenture as Subsidiary Guarantors thereunder to guarantee the payment and performance of the original notes and PAETEC Holding s other obligations under the Indenture.

Joinder Agreement, dated December 6, 2010, pursuant to which PAETEC Holding and the Subsidiary Guarantors under the Indenture were added as parties to the Registration Rights Agreement, dated as of December 2, 2010, by and among the Escrow Issuer and the initial purchasers of the original notes under which PAETEC Holding agreed to use commercially reasonable efforts to file, and cause to be declared effective, a registration statement with the SEC to effectuate the exchange offer described in this prospectus.

As supplemented on December 6, 2010, the Indenture is among PAETEC Holding, the Subsidiary Guarantors party thereto and the Trustee.

Brief Description of Exchange Notes and Guarantees

The exchange notes:

will be general senior unsecured obligations of the Company;

will rank equally in right of payment with all existing and future Senior Indebtedness of the Company, but will be effectively subordinated to all of the Company s existing and future secured Indebtedness to the extent of the value of the collateral that secures such Indebtedness;

will be senior in right of payment to all existing and future Indebtedness of the Company that is subordinated in right of payment to the exchange notes;

will be unconditionally guaranteed, jointly and severally, by each Subsidiary Guarantor; and

will be structurally subordinated to any existing and future Indebtedness and liabilities of Subsidiaries that are not Subsidiary Guarantors.

Each Subsidiary Guarantee of a Subsidiary Guarantor:

will be a general senior unsecured obligation of such Subsidiary Guarantor;

will rank equally in right of payment with all existing and future Senior Indebtedness of such Subsidiary Guarantor, but will be effectively subordinated to all of such Subsidiary Guarantor s secured Indebtedness to the extent of the value of the collateral that secures such Indebtedness; and

will be senior in right of payment to all existing and future Indebtedness of such Subsidiary Guarantor that is subordinated in right of payment to its Subsidiary Guarantee.

As of March 31, 2011, following the closing of the offering of the original notes and our use of the net offering proceeds to pay the merger consideration and other costs and expenses related to our acquisition of Cavalier, we had $1,425 million aggregate principal amount of senior indebtedness outstanding, $675 million of which was senior secured indebtedness.

Principal, Maturity and Interest

The original notes were originally issued in an aggregate principal amount of $450,000,000. The Notes will mature on December 1, 2018.

Interest on the Notes will be payable semi-annually (to holders of record at the close of business on the May 15 or November 15 immediately preceding the interest payment date) on June 1 and December 1 of each year. Interest on the Notes will be computed on the basis of a 360-day year of twelve 30-day months. As described under Registration Rights and Events of Default, the Company may be required to pay additional interest under certain circumstances. All references in the Indenture, in any context, to any interest payable on or with respect to the Notes shall be deemed to include any additional interest payable under such circumstances.

Principal of, premium, if any, and interest on the Notes will be payable, and the Notes may be exchanged or transferred, at the office or agency of the Company in the Borough of Manhattan, The City of New York, or at the corporate trust office of the Trustee, *provided, however*, that, at the Company s option, payment of interest may be made by check mailed to the holders at their addresses as they appear in the security register maintained for the Notes.

The Notes will be issued only in fully registered form, without coupons, in denominations of $1,000 of principal amount and any integral multiple of $1,000. See Book-Entry; Delivery and Form. No service charge will be made for any registration of transfer or exchange of Notes, but the Company may require payment of a fee to cover any transfer tax or other similar governmental charge payable in connection with a registration of transfer or exchange.

The Company may, subject to the covenants described below under the caption Certain Covenants Incurrence of Indebtedness and applicable law, issue additional Notes (Additional Notes) under the Indenture. Any original notes that remain outstanding after the exchange offer, the exchange notes and any Additional Notes subsequently issued would be treated as a single series for all purposes under the Indenture and would be considered Notes for purposes of the provisions of the Indenture summarized in this prospectus.

Subsidiary Guarantees

All obligations of the Company under the Indenture (including, without limitation, the Company s obligations to make payments of principal, interest and premium, if any) with respect to the Notes are and will be guaranteed fully and unconditionally, jointly and severally, by each Subsidiary Guarantor for the ratable benefit of each holder of any outstanding Note from time to time. Under the Indenture, any amount received by the Trustee through the enforcement of any Subsidiary Guarantee will be applied to all outstanding obligations in respect of principal, interest and premium, if any, then owing on the Notes.

If

(1) the Company and its Restricted Subsidiaries have sold their ownership interest in a Subsidiary Guarantor such that it ceases to be a Subsidiary of any such entity, or

(2) a Subsidiary Guarantor has sold all or substantially all its assets,

in each case, in a transaction that complies with the Indenture, then such Subsidiary Guarantor will be released from all of its obligations under its Subsidiary Guarantee. See Certain Covenants Limitation on the Issuance and Sale of Capital Stock of Restricted Subsidiaries and Consolidation, Merger and Sale of Assets.

If the Subsidiary Guarantors have paid, pursuant to enforcement by the Trustee of any Subsidiary Guarantees, the aggregate principal amount of, and accrued and unpaid interest and premium (if any) under, the Notes then outstanding and any other amounts due under the Indenture, then, at such time, all of the Subsidiary Guarantors will be discharged from their Subsidiary Guarantees and all other obligations under the Indenture.

The Indenture provides that the obligations of a Subsidiary Guarantor under its Subsidiary Guarantee will be limited to the maximum amount that will result in the obligations of such Subsidiary Guarantor under its Subsidiary Guarantee not to be deemed to constitute a fraudulent conveyance or fraudulent transfer under federal or state law. See Risk Factors Risks Related to Investing in the Exchange Notes Federal and state fraudulent conveyance laws may permit a court to void the exchange notes and the subsidiary guarantees, and, if that occurs, you may not receive any payments on the exchange notes or the subsidiary guarantees.

The following Subsidiaries are not required to guarantee the Notes:

(1) Subsidiaries, whether now existing or hereafter formed, for which proper regulatory approvals for the incurrence of obligations under Subsidiary Guarantees have not been or cannot be obtained or which otherwise under applicable law may not incur obligations under Subsidiary Guarantees;

(2) at the Company s option, Subsidiaries, in the aggregate, whose assets are less than 5% of the consolidated assets of the Company and its consolidated Subsidiaries as shown on the most recent consolidated financial statements of the Company;

(3) the Mortgage Subsidiary; and

(4) any Receivables Subsidiary.

In addition, if the Company designates a Subsidiary Guarantor as an Unrestricted Subsidiary, which the Company may do under certain circumstances, the designated Subsidiary Guarantor will be released from all of its obligations under its Subsidiary Guarantee.

To the extent that Subsidiaries of the Company are not Subsidiary Guarantors, claims of creditors of such Subsidiaries, including trade creditors, and preferred stockholders, if any, of such Subsidiaries generally will have priority with respect to the assets and earnings of such Subsidiaries over the claims of creditors of the Company, including holders of the Notes. The Notes, therefore, are effectively subordinated in right of payment to the claims of creditors, including trade creditors, and preferred stockholders, if any, of Subsidiaries of the Company formed or acquired in the future that are not Subsidiary Guarantors.

Optional Redemption

Prior to December 1, 2014, the Company may, at its option, in whole or in part, at any time or from time to time, redeem any of the Notes upon not less than 30 nor more than 60 days prior notice mailed by first class mail to each holder s last address as it appears in the security register, at a redemption price equal to 100% of the principal amount thereof plus the Applicable Premium as of, and accrued and unpaid interest, if any, to, but excluding, the redemption date, subject to the rights of holders of Notes on the relevant record date to receive interest due on the relevant interest payment date.

On and after December 1, 2014 and prior to maturity, the Company may, at its option, in whole or in part, at any time or from time to time, redeem any of the Notes upon not less than 30 nor more than 60 days prior notice mailed by first class mail to each holder s last address as it appears in the security register. The Notes will be redeemable at the following redemption prices (expressed in percentages of principal amount), plus accrued and unpaid interest, if any, to, but excluding, the redemption date (subject to the right of holders of record on the relevant regular record date that is on or prior to the redemption date to receive interest due on an interest payment date), if redeemed during the 12-month period commencing on December 1 of the following years:

Year	Redemption Price
2014	104.938%
2015	102.469%
2016 and thereafter	100.000%

In addition, prior to December 1, 2013, the Company may, at its option, at any time or from time to time, redeem up to 35% of the aggregate principal amount of the Notes (including any Additional Notes) with the net proceeds from one or more equity offerings of the Company or, if there is a Parent Transaction, Parent at a redemption price of 109.875% of their principal amount, plus accrued and unpaid interest, if any, to, but excluding, the date of redemption; *provided, however*, that:

Notes representing at least 65% of the principal amount of the Notes (including any Additional Notes) initially issued remain outstanding immediately after each such redemption; and

notice of each such redemption is mailed within 90 days after the closing of the related equity offering.

Table of Contents

In the case of any partial redemption of the Notes, the Trustee will select the Notes for redemption:

in compliance with the requirements of the principal national securities exchange, if any, on which the Notes are listed; or

if the Notes are not listed, by lot or by such other method as the Trustee in its sole discretion deems to be fair and appropriate, except that no Note of $1,000 or less, in original principal amount, will be redeemed in part.

If any Note is to be redeemed in part, the notice of redemption relating to that Note will state the portion of the principal amount of the Note to be redeemed. A new Note in principal amount equal to the unredeemed portion of the Note will be issued in the name of the holder upon cancellation of the original Note.

No Sinking Fund

There will be no sinking fund payments for the Notes.

Certain Covenants

Limitation on Indebtedness

The Company will not, and will not permit any Restricted Subsidiary to, Incur any Indebtedness (other than the Notes issued on the Closing Date, and any Notes exchanged therefor or for Additional Notes under the terms of the Indenture and the Registration Rights Agreement, and any other Existing Indebtedness); *provided, however*, that the Company and any Subsidiary Guarantor may Incur Indebtedness if, after giving effect to the Incurrence of such Indebtedness and the receipt and application of the proceeds therefrom, the Consolidated Leverage Ratio of the Company would be greater than zero and less than 4.75:1.0.

Notwithstanding the foregoing, the Company and any Restricted Subsidiary (except as specified below) may Incur each and all of the following:

(1) Indebtedness incurred under Credit Agreements outstanding at any time in an aggregate principal amount not to exceed $115.0 million, less the aggregate amount of all Net Cash Proceeds of Asset Sales applied to permanently repay any such Indebtedness pursuant to the covenant described below under Limitation on Asset Sales ;

(2) Indebtedness owed:

(A) to the Company; or

(B) to any Restricted Subsidiary; *provided, however*, that any such Indebtedness of the Company or a Subsidiary Guarantor owing to a Restricted Subsidiary that is not a Subsidiary Guarantor is expressly subordinated in right of payment to the Notes or the Subsidiary Guarantee, as the case may be; *provided, further*, that any event which results in any such Restricted Subsidiary ceasing to be a Restricted Subsidiary or any subsequent transfer of such Indebtedness (other than to the Company, another Restricted Subsidiary or the holder of a Lien permitted by the Indenture) will be deemed, in each case, to constitute an Incurrence of such Indebtedness not permitted by this clause (2);

(3) Indebtedness issued in exchange for, or the net proceeds of which are used to refinance or refund, then outstanding Indebtedness (other than Indebtedness Incurred under clause (1), (2), (4) or (10) of this paragraph) and any refinancings thereof in an amount not to exceed the amount so refinanced or refunded (plus premiums, accrued interest, fees and expenses); *provided, however*, that Indebtedness the proceeds of which are used to refinance or refund the Notes or Indebtedness that is *pari passu* in right of payment with, or subordinated in right of payment to, the Notes shall only be permitted under this clause (3) if:

(A) in case the Notes or any Subsidiary Guarantees are refinanced in part or the Indebtedness to be refinanced is *pari passu* in right of payment with the Notes or any Subsidiary Guarantees, such new

124

Indebtedness, by its terms or by the terms of any agreement or instrument pursuant to which such new Indebtedness is outstanding, is expressly made *pari passu* in right of payment with, or subordinate in right of payment to, the remaining Notes or such Subsidiary Guarantees, as applicable;

(B) in case the Indebtedness to be refinanced is subordinated in right of payment to the Notes or any Subsidiary Guarantee, such new Indebtedness, by its terms or by the terms of any agreement or instrument pursuant to which such new Indebtedness is issued or remains outstanding, is expressly made subordinate in right of payment to the Notes or such Subsidiary Guarantee, as applicable, at least to the extent that the Indebtedness to be refinanced is subordinated in right of payment to the Notes or such Subsidiary Guarantee, as applicable; and

(C) such new Indebtedness, determined as of the date of Incurrence of such new Indebtedness, does not mature prior to the Stated Maturity of the Indebtedness to be refinanced or funded, and the Average Life of such new Indebtedness is at least equal to the remaining Average Life of the Indebtedness to be refinanced or refunded; and *provided, further*, that in no event may the Company s Indebtedness be refinanced by means of any Indebtedness of any of its Restricted Subsidiaries pursuant to this clause (3);

(4) Indebtedness:

(A) under Currency Agreements and Interest Rate Agreements; *provided, however*, that such agreements are:

(i) designed to protect the Company or the Restricted Subsidiaries against fluctuations in foreign currency exchange rates or interest rates and not for speculative purposes; and

(ii) do not increase the Indebtedness of the obligor outstanding at any time other than as a result of fluctuations in foreign currency exchange rates or interest rates or by reason of fees, indemnities and compensation payable thereunder; or

(B) arising from agreements providing for indemnification, adjustment of purchase price or similar obligations, or from Guarantees or letters of credit, surety bonds or performance bonds securing any of the Company s obligations or those of any of its Restricted Subsidiaries pursuant to such agreements, in any case Incurred in connection with the purchase or disposition of any business, assets or Restricted Subsidiary (other than Guarantees of Indebtedness Incurred by any Person acquiring all or any portion of such business, assets or Restricted Subsidiary for the purpose of financing such acquisition), in a principal amount not to exceed the gross proceeds actually received by the Company or any Restricted Subsidiary, as applicable, in connection with such purchase or disposition;

(5) Indebtedness of the Company and Guarantees thereof, to the extent the net proceeds thereof are promptly:

(A) used to purchase Notes tendered in an Offer to Purchase made as a result of a Change of Control; or

(B) deposited to defease the Notes as described below under Defeasance ;

(6) Guarantees of the Notes and Guarantees by the Company or any Restricted Subsidiary of Indebtedness of the Company or another Restricted Subsidiary that was permitted to be Incurred by another provision of this covenant; *provided* that if the Indebtedness being Guaranteed is subordinated in right of payment to the Notes or a Subsidiary Guarantee, then such Guarantee shall be subordinated in right of payment to the Notes or such Subsidiary Guarantee to the same extent as the Indebtedness Guaranteed; and *provided, further*, that only the Company and Subsidiary Guarantors may Guarantee Indebtedness Incurred pursuant to the first paragraph of this covenant;

(7) Indebtedness Incurred to finance or refinance the cost (including the cost of design, development, acquisition, construction, installation, improvement, transportation or integration and all transaction costs related to the foregoing) to acquire equipment, inventory or network assets (including acquisitions by way

of Capitalized Lease Obligations and acquisitions of the Capital Stock of a Person that becomes a Restricted Subsidiary to the extent of the fair market value of the equipment, inventory or network assets so acquired, plus goodwill associated therewith) by the Company or a Restricted Subsidiary after the Closing Date; *provided, however*, that the aggregate principal amount of such Indebtedness outstanding at any time may not exceed the greater of $50 million and 3.5% of Total Assets at the time of Incurrence;

(8) Non-Recourse Indebtedness of the Mortgage Subsidiary Incurred to finance the purchase of the Company s headquarters buildings and related real and personal property in an aggregate principal amount not to exceed $35 million (and Non-Recourse Indebtedness of the Mortgage Subsidiary issued in exchange for, or the net proceeds of which are used to refinance or refund, then outstanding Indebtedness Incurred pursuant to this clause (8));

(9) Acquired Indebtedness; *provided, however*, that after giving effect to the Incurrence of such Indebtedness pursuant to this clause (9) and the related acquisition transaction, either (a) the Company would have been able to Incur $1.00 of Indebtedness under the first paragraph of this covenant or (b) the Company s Consolidated Leverage Ratio would not be greater than such ratio immediately prior to such acquisition transaction;

(10) Indebtedness under Shareholder Subordinated Notes;

(11) Indebtedness Incurred by a Receivables Subsidiary in a Qualified Receivables Financing that is not recourse to the Company or any Restricted Subsidiary other than a Receivables Subsidiary (except for Standard Securitization Undertakings); and

(12) Indebtedness (in addition to Indebtedness permitted under clauses (1) through (11) above) in an aggregate principal amount outstanding at any time not to exceed $35 million.

Notwithstanding any other provision of this Limitation on Indebtedness covenant, the maximum amount of Indebtedness that the Company or a Restricted Subsidiary may Incur pursuant to this Limitation on Indebtedness covenant shall not be deemed to be exceeded with respect to any outstanding Indebtedness due solely to the result of fluctuations in the exchange rates of currencies.

For purposes of determining any particular amount of Indebtedness under this Limitation on Indebtedness covenant, (i) Guarantees, Liens or obligations with respect to letters of credit supporting Indebtedness otherwise included in the determination of such particular amount of Indebtedness shall not be included, (ii) any Liens granted pursuant to the equal and ratable provisions referred to in the Limitation on Liens covenant shall not be treated as Indebtedness and (iii) the consummation of the Assumption shall not constitute the Incurrence of additional Indebtedness.

For purposes of determining compliance with this Limitation on Indebtedness covenant, in the event that an item of Indebtedness meets the criteria of more than one of the types of Indebtedness described in the above clauses, the Company, in its sole discretion, shall classify, and from time to time may reclassify, such item of Indebtedness and only be required to include the amount and type of such Indebtedness in one of such clauses; *provided, however*, that the Company need not classify such item of Indebtedness solely by reference to one provision permitting such Indebtedness, but instead may classify such item of Indebtedness in part by reference to one such provision and in part by reference to one or more other provisions of this covenant; *provided, further*, that Indebtedness under Credit Agreements outstanding on the Closing Date will be deemed to have been Incurred on such date in reliance on the exception provided by clause (1) of the second paragraph of this covenant.

Neither the Company nor any Subsidiary Guarantor will Incur any Indebtedness that pursuant to its terms is subordinated or junior in right of payment to any Indebtedness unless such Indebtedness is subordinated in right of payment to the Notes or the relevant Subsidiary Guarantee, as applicable, to the same extent; *provided* that Indebtedness will not be considered subordinated or junior in right of payment to any other Indebtedness solely by virtue of being unsecured or secured to a greater or lesser extent or with greater or lower priority.

Limitation on Restricted Payments

The Company will not, and will not permit any Restricted Subsidiary to, directly or indirectly:

(1) declare or pay any dividend or make any distribution on or with respect to its Capital Stock (other than (A) dividends or distributions payable solely in shares of the Company s Capital Stock (other than Disqualified Stock) or in options, warrants or other rights to acquire shares of such Capital Stock (other than Disqualified Stock); and (B) pro rata dividends or distributions on Common Stock of Restricted Subsidiaries held by minority stockholders) held by Persons other than the Company or any Restricted Subsidiary;

(2) purchase, redeem, retire or otherwise acquire for value any shares of Capital Stock of:

(A) the Company or an Unrestricted Subsidiary (including options, warrants or other rights to acquire such shares of Capital Stock) held by any Person; or

(B) a Restricted Subsidiary (including options, warrants or other rights to acquire such shares of Capital Stock) held by any Affiliate of the Company (other than a Wholly Owned Restricted Subsidiary) or any holder (or any Affiliate of such holder) of 5% or more of the Company s Capital Stock;

(3) make any voluntary or optional principal payment, or voluntary or optional redemption, repurchase, defeasance, or other acquisition or retirement for value, of any Indebtedness that is subordinated in right of payment to the Notes or any Subsidiary Guarantee (other than Indebtedness Incurred under clause (2) of the second paragraph of the Limitation on Indebtedness covenant); or

(4) make any Investment, other than a Permitted Investment, in any Person;

(such payments or any other actions described in clauses (1) through (4) above being collectively called Restricted Payments) if, at the time of, and after giving effect to, the proposed Restricted Payment:

(A) a Default or Event of Default shall have occurred and be continuing;

(B) the Company could not Incur at least $1.00 of Indebtedness under the first paragraph of the Limitation on Indebtedness covenant; or

(C) the aggregate amount of all Restricted Payments (the amount, if other than in cash, to be determined in good faith by the Board of Directors of the Company, whose determination shall be conclusive and evidenced by a board resolution) made after the Closing Date shall exceed the sum of:

(i) the amount by which Consolidated EBITDA of the Company exceeds 140% of Consolidated Interest Expense of the Company, in each case determined on a cumulative basis during the period (taken as one accounting period) beginning on October 1, 2010 and ending on the last day of the last fiscal quarter preceding the Transaction Date for which reports have been filed with the SEC or provided to the Trustee pursuant to the SEC Reports and Reports to Holders covenant; *plus*

(ii) the aggregate Net Cash Proceeds and the fair market value of all non-cash proceeds received by the Company after October 1, 2010 from the issuance and sale permitted by the Indenture of its Capital Stock (other than Disqualified Stock) to a Person who is not a Subsidiary of the Company, including an issuance or sale permitted by the Indenture of Indebtedness of the Company for cash subsequent to October 1, 2010 upon the conversion of such Indebtedness into the Company s Capital Stock (other than Disqualified Stock), or from the issuance to a Person who is not a Subsidiary of the Company of any options, warrants or other rights to acquire Capital Stock of the Company (exclusive of any Disqualified Stock or any options, warrants or other rights that are redeemable at the option of the holder, or are required to be redeemed, prior to the Stated Maturity of the Notes); *plus*

(iii) an amount equal to the net reduction in Investments (other than reductions in Permitted Investments) in any Person resulting from payments of interest on Indebtedness, dividends, repayments of loans or advances, or other transfers of assets, in each case to the Company or any Restricted