Section 3(1) and Section 271. Throughout this extended exchange of opinions – both between AT&T and Bell Atlantic/GTE on the one hand, and between my colleague Professor Coffee and me on the other – reference has been made both to regulatory schemes in which the *acquisition* of an option is treated as the jurisdictional trigger and to regulatory schemes in which *exercise* of an option triggers jurisdiction. There is only one principled basis for deciding which regulatory scheme is relevant here: the purpose of Section 271 of the Federal Communications Act.

4. As I have urged throughout this exchange, whether an option should be treated as the equivalent of a current equity interest (and acquiring the option therefore treated as the jurisdictional trigger) or whether the exercise of the option should trigger jurisdiction, *depends on the purpose of the particular statute*. Where the statutory purpose is implicated by the acquisition of an option, having the option is treated as the triggering event. Where the statutory purpose is implicated only by the exercise of the option, then it is only the exercise that triggers jurisdiction.

5. The Federal Securities laws, referred to repeatedly by AT&T and Professor Coffee, and the Hart-Scott-Rodino Pre-Merger Notification Act, referred to by Bell Atlantic/GTE and me, illustrate the dichotomy. As I described in my Supplemental Declaration, the portions of the Federal Securities law relied upon by AT&T all involve statutory purposes that necessitate treating the acquisition of options as a jurisdictional trigger. In the case of insider trading and disclosure under the tender offer rules, options pose the same problem as do the underlying securities; the statutory purpose thus dictates treating the purchase or sale of an option as the transfer of an equity interest. In contrast, the Hart-Scott-Rodino Pre-Merger Notification Act is concerned with the exercise of control that requires acquisition of formal corporate participation rights. Accordingly,

acquisition of an option does not trigger reporting under Hart-Scott-Rodino; only *exercise* of an option subjects the transaction to the Act's reporting requirements.

6. This discussion places AT&T's repeated, but inaccurate, references to "stock parking" in their proper context. The term grows out of an unlawful practice that sought to avoid the disclosure requirements of Section 13d of the Securities Exchange Act of 1934 (the "Exchange Act"). Section 13d requires that shareholders who acquire more than 5 percent of the outstanding shares of any class of securities registered under the Exchange Act disclose both the amount of their holdings and their plans with respect to the company. Because disclosure under Section 13d typically results in an increase in the market price of the shares, acquirers who would like to acquire more shares have an incentive to avoid disclosure, and thereby avoid the price increase. This can be accomplished by having someone else acquire – i.e., "park"– in their name the shares that would trigger disclosure if acquired in the name of the real acquiring shareholder. As indicated in Paragraph 4, a disclosure statute like Section 13d treats options as a jurisdictional trigger because their acquisition implicates the statutory purpose – broad disclosure. Despite AT&T's hyperbole, NewCo's DataCo option has nothing to do with stock parking. The purpose of Section 271, unlike that of Section 13d, is not implicated until the option is exercised.

7. For purposes of Section 271 of the Federal Communications Act, then, an option adds nothing to a party's capacity to participate through ownership of an equity interest in the provision of long distance services. Only the exercise of that option – the transformation of a future equity interest into a *current* equity interest – conveys the equity attributes necessary to implicate Section 271 concerns. As with Hart-Scott-

Rodino, exercise of the option – but not the option's acquisition – independently triggers the application of the regulatory scheme.

8. In its May 5th Opposition, AT&T raises yet another scheme that it asserts exposes an option as an equity interest. This time AT&T points to the definitions of the terms "equity interest" and "equity security" contained in Sections 1.19 and 1.20 of the American Law Institute's Principles of Corporate Governance,[1] of which both Professor Coffee and I were reporters. Section 1.19 defines an "equity interest" as including an "equity security," and Section 1.20 defines an "equity security" as "a security convertible ... into a [share in a corporation]." On this basis, AT&T asserts that the ALI Principles treat a stand-alone option as an equity interest. Here, however, AT&T misstates the application of the ALI Principles.

(i) Convertible common stock, like other stock, is an equity interest. NewCo's Class B convertible common stock, for example, represents a 9.5 percent equity interest in DataCo. But as I made clear in my initial declaration, as a matter of economic substance a convertible security is composed of two elements: a current equity interest in the form of stock carrying voting and distribution rights, and an option – a future equity interest that becomes a current equity interest only when exercised. What is at stake in this matter is whether the *option* component is an *additional* equity interest, and therefore must be separately counted in determining whether NewCo owns more than 10 percent of

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[1] While AT&T refers to the ALI Principles as a "'restatement' of corporate law," the American Law Institute was at some pains to distinguish the project from a Restatement. From the inception of the project, whether to characterize the ALI Principles as a "restatement" has been controversial. The difference is that a Restatement is directed at court made law, while significant elements of the ALI Principles would require implementation by the legislature. Chief Reporter's Foreword, I American Law Institute, Principles of Corporate Governance: Analysis and Recommendations XXV-XXVI. While the ALI Principles do not directly address whether Sections 1.19 and 1.20 are of Restatement character, since Section 1.19 is described as "new," and Section 1.20 states that its source is statutory, the two sections would not appear to be "restatement-like."

DataCo for purposes of section 3(1). On this issue, the ALI Principles explicitly disclaim the position that a stand-alone option is an equity interest.

(ii) Under Section 7.02(a) of the ALI Principles, the holder of an "equity security" has standing to bring a derivative suit. If AT&T is correct that under the ALI Principles a stand-alone option is an equity security (and therefore also an equity interest), then, tautologically, the holder of a stand-alone option must have standing to bring a derivative suit. In fact, the ALI Principles disclaim precisely this result. Paragraph c of the comment to section 7.02 states that "Section 7.02(a) takes no position on whether the holder of a warrant or right issued by the corporation and not attached to some other security should have standing to bring a derivative action." On this issue, state corporate law is clear – an option holder lacks an equity interest and therefore does not have standing to bring a derivative suit, and the ALI Principles decline to take a contrary position. Until exercised, NewCo's option adds no additional equity interest to NewCo's initial 9.5 percent interest in DataCo.

9. The American Law Institute's reluctance to treat stand-alone options as an equity interest, and thereby confer standing to bring a derivative suit on its holder, is consistent with the general structure of corporate law: only exercise of an option confers equity rights on its holder. Corporate fiduciary principles provide a compelling illustration. Directors owe equity holders a fiduciary duty. *Directors do not owe option holders a fiduciary duty.* [2] And that proposition brings us full circle, to the argument in

[2] *See Glinert v. Wickes Cos.*, 1990 WL 34703, at *9 (Del.Ch. Mar. 27, 1990)("Under our law, the option feature of these instruments does not qualify for the protections that flow from a fiduciary duty."); *Powers v. British Vita, P.L.C.*, 969 F. Supp. 4, 6 (S.D.N.Y. 1997)("Clearly, any attempt to analogize options to stocks in order to suggest a fiduciary duty are to no avail."); *Simons v. Cogan*, 549 A.2d 300, 303 (Del. 1988)("[A] mere expectancy does not create a fiduciary duty."); *Starkman v. Warner Communications, Inc.*, 671 F. Supp. 297, 304 ("The [option] instrument stands alone, claiming no equity in the corporation, entitled to no vote, and with no fiduciary obligation of the management to the option holder's interest.").

my Initial Declaration: "[F]or corporate law purposes the boundary between an equity security and an option is quite explicit and sharp. Only the exercise of the option transmutes the holder's interest into an equity interest with corporate participation rights." Initial Declaration ¶16. And that proposition brings us full circle, to the argument in my Initial Declaration: "[F]or corporate law purposes the boundary between an equity security and an option is quite explicit and sharp. Only the exercise of the option transmutes the holder's interest into an equity interest with corporate participation rights." Initial Declaration ¶16.

10. Also in its May 5th Opposition, AT&T advances what appears to be a new argument for why an option is really an equity interest. Citing the article for which Merton Miller and Franco Modigliani were awarded the Nobel Prize in Economic Science,[3] AT&T asserts that "financial theory teaches that a firm's capital is in the form of either equity or debt." May 5th Opposition ¶ 2, p.21. The point, I suppose, is that an option must be one or the other; not being debt, it must be equity. While I am aware of no basis for AT&T's proposition that the issuance of an option or a warrant must be either debt or equity, Professors Miller's and Modigliani's seminal article certainly provides no support for it (or, indeed, even bears on the claim). That article advanced, what are called in financial economics, the "Irrelevancy Propositions" – in effect, that a firm's cost of capital is not affected by the mix of debt and equity in its capital structure and that the value of the firm is unaffected by whether the firm finances an investment with retained earnings or instead pays a dividend and finances the investment with debt. In other words, debt and equity are equivalent for valuation purposes. The FCC, of

[3] Merton Miller and Franco Modigliani, The Cost of Capital, Corporation Finance and the Theory of Investment, 48 Am. Econ. Rev. 261 (1958).

course, does not equate debt and equity and, in fact, neither do Professors Miller and Modigliani. The Irrelevance Propositions were intended as an extreme null hypothesis, much of the last 40 years of financial economics scholarship having been devoted to demonstrating why the Irrelevancy Propositions are incorrect.[4] For example, Miller and Modigliani did not take the governance characteristics of debt and equity into account, precisely the characteristics of greatest interest to the FCC. Indeed, if it is finance with which we are concerned, equity is valued by quite different methods than options. Variants of the capital asset pricing model or arbitrage pricing model are typically invoked for the pricing of equity. The Black-Scholes option pricing model is typically invoked to price options and option-like instruments such as warrants and conversion rights.

NewCo's Receipt of Its Opportunity Cost in the Event of Sale Does Not Result in NewCo Improperly Receiving Pre-Approval Appreciation in DataCo's InterLATA Data Business

11. AT&T appears to argue that the terms of DataCo's option will nevertheless result in a violation of Section 271 because the option allows NewCo to profit from pre-exercise appreciation in the value of DataCo: through receipt, in the event of a sale of Class B shares, by NewCo of its opportunity cost with respect to Section 271 compliance greater than 50 percent but less than 95 percent. AT&T's analysis, however, confuses payment of what NewCo would have earned had it *not* invested in DataCo, with a payment based on DataCo's performance.

12. Under the DataCo option, if NewCo eliminates applicable section 271 restrictions on at least 50% but less than 95% of Bell Atlantic in-region lines, its Class B

[4] The Irrelevancy Propositions are developed in accessible fashion in Jesse Choper, John C. Coffee, Jr., and Ronald J. Gilson, Cases and Materials on Corporations ch. 3 (5th ed. 2000).

shares will be convertible into 80 percent of DataCo's shares (assuming no dilution), but NewCo can retain only those convertible shares that would be convertible into 10 percent of DataCo's outstanding shares. In addition, NewCo cannot retain all the proceeds from any sale of the shares convertible above 10% that it must sell; it can retain only the value of NewCo's initial investment in the shares sold plus the amount NewCo would have earned had it placed the remainder of its initial investment in an *S & P 500 Index fund* instead of the DataCo option – that is, NewCo's "opportunity cost." AT&T argues that Section 271 approval grants NewCo the right to earn profits from long distance services after approval but not before; return of NewCo's opportunity cost, the argument runs, therefore gives it an improper pre-approval profit from long distance services.

13. This argument simply ignores the fact that NewCo's opportunity cost is measured, properly, by what NewCo would have earned in another investment, which, as Professor Coffee correctly points out, is best approximated by the S & P 500 Index used in the Revised Proposal. For NewCo to participate in profits from *DataCo*'s pre-approval provision of long distance service, the payment would have to be keyed to *DataCo*'s performance, not NewCo's performance measured by the S & P 500 Index. DataCo is an Internet backbone firm, whose stock performance can be expected to track an Internet index, not the S & P 500 Index.[5] Thus, payment measured by NewCo's

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[5] The relevant determinant of DataCo's performance is the risk and return of its business, not its initial public offering. Professor Coffee accurately describes studies that, lumping all types of initial public offerings together, show average underperformance over a sustained period, Third Declaration of Professor John C. Coffee, Jr. ¶8 ("Coffee Third Declaration"). However, Professor Coffee neglects to mention the results of more recent studies that differentiate between the types of issuers in initial public offerings. These studies show that the sustained underperformance to which Professor Coffee refers is a phenomenon of small-firm IPOs; large-firm IPOs – like that contemplated for DataCo – do not experience this pattern. Indeed, recent studies show that this underperformance is not an IPO phenomenon at all. Rather, small firms underperform the market regardless of the existence of a recent IPO.

opportunity cost rather than DataCo's performance is not a payment of profits from the provision of long distance services.

14. AT&T also argues that the fact that the exercise price of NewCo's option is fixed alone constitutes a violation of Section 271 because, unless this price fluctuates with DataCo's appreciation, NewCo receives the benefit of DataCo's pre-exercise performance. In AT&T's analysis, a Bell Operating Company ("BOC") can only buy a long distance carrier at market price so that it obtains no benefit from appreciation in value resulting from the long distance carrier's prior performance. AT&T May 5th Opposition ¶3. The argument clearly proves too much. To take AT&T's example, suppose a BOC, believing it has satisfied Section 271, enters into an executory agreement calling for the acquisition of a long distance carrier at a price negotiated at the time of execution. There follows a lengthy approval process – perhaps prolonged by objections from AT&T – that results in Section 271 approval two years later. In the interim, the value of the long distance carrier appreciates. AT&T's analysis suggests that the BOC in this case would be prohibited from completing the transaction under the negotiated terms because, if the BOC were to purchase the carrier at the negotiated price, *it* would profit by the difference between the negotiated and then-current market price. As a result, every fixed-price acquisition agreement that is closed after some delay potentially violates Section 271 if, during that delay, the long distance carrier's stock appreciates. There is simply no basis for this bizarre result.

15. Indeed, AT&T's argument appears to invalidate its own acquisition of MediaOne. That acquisition agreement was signed over a year ago, during which time the market value of MediaOne has undoubtedly appreciated. Presumably, AT&T is prevented from profiting as a result of pre-approval MediaOne performance. However,

AT&T does not represent in its opposition that it intends to increase the consideration it has agreed to pay for MediaOne.

NewCo Will Not Control DataCo By Virtue of Its Option

16. Finally, AT&T argues again that even if NewCo's option is not tautologically an equity interest under Section 3(1), the option and the associated pre-conversion consent rights result in NewCo exercising actual control of DataCo and therefore renders DataCo a NewCo affiliate under Section 3(1). For the purpose of this inquiry, the FCC must confront the policy of the statute and the practicalities of transactional practice. As I showed in my initial Declaration, the FCC's treatment of an equivalent transactional structure – the option held by the acquiring company in connection with a regulated acquisition during the post-execution/pre-FCC approval and closing period – plainly reflects this reality. After execution, the acquiring company holds an option to purchase the target company at the price specified in the acquisition agreement, with exercise of the option conditioned on FCC approval. During the period prior to FCC approval and closing, the acquiring company has the right to all appreciation in the value of the target company. Also during this period, the acquiring company typically has the benefit of a set of covenants, just like the consent requirements associated with NewCo's option, that restrict the target's behavior without acquiring-company consent. Similarly, the incentives that AT&T ascribes to DataCo management during the pre-conversion period are equally applicable to target management during the post-execution/pre-FCC approval and closing period.

17. Thus, if AT&T's argument is to be taken seriously, any acquisition that takes the standard form will violate FCC approval rights because, as a result of the inherent option, the target will be controlled by the acquiring company and will therefore

be the acquiring company's affiliate under Section 3(1). For example, AT&T has been in this position for a full year with respect to its MediaOne acquisition.

18. What is apparent is that the FCC has thoughtfully exercised its discretion to develop a practical approach to control under Section 3(1), one that allows the construction of transactional structures bridging the period pending Commission approval so long as the structure does not implicate the matters of concern under the relevant statutory structure. The NewCo/DataCo option structure does not allow NewCo to get the benefit of service bundling without FCC approval. Accordingly, the NewCo/DataCo option structure should be treated the same as functionally equivalent option structures, including AT&T/Media One's option structure. In the end, the FCC is presiding over the restructuring and consolidation of the U.S. telecommunications industry. Managing that process effectively requires the thoughtful review of new transactional structures that preserve FCC approval over those matters of substance under Section 271.

I declare under penalty of perjury that the foregoing is true and correct.

Date: May 10, 2000

Ronald J. Gilson

C

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
GTE CORPORATION,	)	
	)	
Transferor,	)	
	)	
and	)	CC Docket No. 98-184
	)	
BELL ATLANTIC CORPORATION,	)	
	)	
Transferee,	)	
	)	
For Consent to Transfer Control	)	

DECLARATION OF PAUL R. GUDONIS

1. My name is Paul R. Gudonis, and I am Genuity's Chief Executive Officer. As CEO, I have ultimate responsibility for the development and implementation of Genuity's business plan. I am also responsible for managing all of Genuity's business units, including those providing Internet access, network management, web hosting, network security, and electronic commerce services to business and ISP customers. I have worked for Genuity (formerly GTE Internetworking and BBN Corporation) since 1994 and, prior to GTE's acquisition of BBN in mid-1997, served as President of BBN's Internet Services division. Contrary to AT&T's view, I can therefore attest that my loyalty has been -- and will continue to be -- to Genuity (whatever its name), and that Genuity (one of the firms involved in the Internet's creation) does have a "separate pre-existing business plan" and a "distinct corporate culture."[1]

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[1] Opposition of AT&T Corp. to Applicants' Revised Proposal Regarding GTE's InterLATA Operations, at 6 (May 5, 2000).

2. I am familiar with the investor safeguards detailed in Revised Exhibit C, attached to the submission Bell Atlantic/GTE ("NewCo") is today filing with the Commission. These safeguards provide that a vote of NewCo's Class B shares or NewCo's consent is required for certain extraordinary actions -- for example, a sale of all Genuity assets or an amendment to Genuity's charter. These investor safeguards will not impede in any way the implementation of Genuity's five-year business plan. Neither a vote of NewCo's Class B shares nor NewCo's consent will be required to implement Genuity's five-year business plan in full.

3. Likewise, I am familiar with the transitional contracts that Genuity and NewCo have negotiated for the supply of certain services -- for example, real estate and employee benefits support. These contracts include a number of features that ensure Genuity's complete independence from NewCo; indeed, these temporary contracts are essential to Genuity's ability to operate as a viable independent business during its transition away from reliance on GTE's centralized systems. *First*, these contracts are all for terms of no more than one year, and Genuity may terminate them at any time without penalty. *Second*, these contracts all govern services that Genuity could, after a reasonable transition, either provide internally or out-source to a third party. *Third*, these contracts cannot be renewed after their one-year expiration unless the Chief of the FCC's Common Carrier Bureau does not object to their renewal. The cumulative effect of these factors, along with the fiduciary duty Genuity's Board owes to its public shareholders, ensures that Genuity will switch providers of these contractually specified services if doing so would give Genuity a better deal.

I declare under penalty of perjury that the foregoing is true and correct.

Dated: May 9, 2000

Paul R. Gudonis

D

REVISED EXHIBIT A

GENUITY ESTABLISHED AS INDEPENDENT PUBLIC CORPORATION

Bell Atlantic and GTE will eliminate any section 271 issue that could arise from Bell Atlantic's ownership of Genuity (formerly known as GTE Internetworking) through the following structure.

1. IPO of Genuity

Genuity's existing nationwide data business will be established as a separate corporation that will be publicly owned and controlled. Before merging with Bell Atlantic, GTE will exchange its common stock of Genuity for shares of a new class of common stock, the Class B common stock, and Genuity will sell 90.5% of its equity to public shareholders through an initial public offering ("IPO"). Following these transactions, the Class B stock will carry only a 9.5% equity interest (9.5% of the voting rights and the right to receive 9.5% of any dividends or other distributions) in Genuity, subject to the conversion rights and investor safeguards described below, and Genuity's Class A common stock, initially representing 90.5% of the equity interest in the company, will be owned by the public. The merger of Bell Atlantic and GTE (creating "NewCo") will not close until the IPO is completed.

2. Conversion Rights

The extent of NewCo's rights to convert its Class B stock into a greater equity interest is as described below. NewCo will have five years from the closing of the merger (or longer, under certain specified circumstances) to satisfy the conditions associated with its conversion rights and to exercise those conversion rights.

A. *No Conversion Right Above 10% Equity Interest If Threshold Not Met*

Unless and until NewCo eliminates, as to at least 50% of Bell Atlantic in-region lines,[1] section 271 restrictions applicable to its operation of Genuity's business, NewCo will only have the right to convert its Class B stock into Class A stock representing a 10% equity interest in Genuity. Accordingly, if NewCo fails to meet the 50% threshold within the conversion period, NewCo will never have any right to convert its stock into more than a 10% interest, and the public shareholders' ownership of at least 90% of the company will be permanent. Likewise, if NewCo transfers its Class B shares to a third party before reaching the 50% section 271 threshold, that third party will never be able to convert those shares into more than a 10% interest in Genuity.

[1] "Bell Atlantic in-region lines" shall equal the sum of the number of lines for each of the Bell Atlantic in-region states, and the number of lines for each Bell Atlantic state shall be the number of total billable access lines for the Bell Atlantic operating company in that state in Bell Atlantic's 1999 ARMIS reports, except that because the entry for Bell Atlantic–New York Telephone includes Bell Atlantic lines in both New York and Connecticut, the number of lines for Connecticut shall be 54,087 and the number for New York shall be 11,088,712.

B. *Conversion Right Above 10% Equity Interest Once Threshold Is Met*

Once NewCo has met the 50% section 271 threshold, its Class B shares will be convertible into stock that will represent 80% of the outstanding shares of Genuity following conversion, assuming no additional Class A shares are issued before conversion. Even after meeting this threshold, however, NewCo itself cannot exercise its conversion rights so as to own and control Genuity unless and until NewCo has eliminated all section 271 restrictions applicable to NewCo's operation of Genuity's business.

Once NewCo has eliminated such restrictions as to 95% of Bell Atlantic in-region lines, NewCo may require Genuity to reconfigure its operations in one or more Bell Atlantic in-region states where NewCo has not eliminated such restrictions in order to bring those operations into compliance with section 271 and allow NewCo to exercise its option and own and operate Genuity, *provided that* (i) NewCo gives the Commission at least 90 days advance notice of its intent to exercise its option and submits to the Chief of the Common Carrier Bureau a plan for the reconfiguration of Genuity's operations in the relevant state or states, (ii) the reconfiguration of Genuity's operations does not result in the loss to Genuity of more than 3% of its annual revenue, and (iii) NewCo reimburses Genuity for the cost of such reconfiguration (as provided for in an agreement between NewCo and Genuity).

NewCo's post-conversion interest will be lower than 80% if Genuity, as is anticipated, issues additional shares of Class A stock before NewCo exercises its conversion rights. Upon exercise of its conversion rights, NewCo's Class B shares shall be converted into the appropriate number of Class C shares. Each share of Class C stock will be identical to a share of Class A stock except that it will carry five votes; these enhanced voting rights will likely preserve NewCo's ability to obtain voting control of Genuity post-conversion in the event Genuity has issued substantial amounts of new Class A shares. If NewCo transfers its Class B shares to another party, that party may only convert them into Class A stock.

Subject to the limitation on sales proceeds below, NewCo will have the right at any time after it has met the 50% section 271 threshold to dispose of all or part of its Class B shares, or to exercise its conversion rights as part of a transaction by which it immediately disposes of all or part of its interest in Genuity so that its post-conversion interest in Genuity does not exceed a 10% equity interest. To the extent Class B shares are purchased by someone who is not subject to applicable section 271 restrictions, that purchaser would be free to convert those Class B shares immediately into Class A shares. If at the time NewCo's conversion period would otherwise expire, NewCo has a pending contract to sell its Class B shares to such a purchaser, the conversion period will be extended to allow for completion of the sale and the purchaser's immediate conversion.

C. *Limitation on Sales Proceeds*

If NewCo sells all of its stock before it has eliminated applicable section 271 restrictions as to 95% of Bell Atlantic in-region lines, NewCo will not have a right to retain after-tax sale proceeds that exceed (i) the value of a 10% equity interest in Genuity (determined based on the sale proceeds), plus (ii) the amount NewCo would have if it had taken the amount of its initial investment in Genuity above a 10% interest (based on the IPO offering price for the Class A shares) and invested it at the time of closing in the S&P 500 Index. If, during such period, NewCo sells all of its stock except an amount convertible into a 10% equity interest in Genuity, NewCo will have a right to retain only the amount described in clause (ii) above.[2] In each of these cases, NewCo would pay the remainder of its after-tax sale proceeds, or such lesser amount as the Commission in its discretion may determine, into the general fund of the U.S. Treasury. Once NewCo has eliminated applicable section 271 restrictions as to at least 95% of Bell Atlantic's in-region lines, NewCo may sell its stock and retain the full sale proceeds.

D. ***Extension of Five-Year Conversion Period***

If, by the end of five years, NewCo has eliminated applicable section 271 restrictions as to all but 10% of Bell Atlantic in-region lines (or as to all but one state, irrespective of the percentage of Bell Atlantic in-region lines accounted for by that state, plus additional states accounting for up to 5% of Bell Atlantic in-region lines), NewCo may file a petition with the Commission requesting relief, in the event of which filing NewCo will be permitted one additional year (which may be extended at the discretion of the Commission) in which to eliminate the remaining restrictions and exercise its conversion rights. If, by the end of the conversion period, litigation is pending over whether NewCo has eliminated such restrictions as to certain lines, and if a court determines after the end of the conversion period that NewCo has eliminated such restrictions as to those lines, then for purposes of these provisions NewCo shall be deemed to have eliminated those restrictions within the conversion period and shall be permitted a reasonable time to exercise or dispose of its conversion rights.

The Commission shall have discretion to toll or extend the running of the conversion period to account for intervening events that delay elimination of section 271 restrictions.

E. ***Compliance with Legal Order***

If, before NewCo satisfies the 50% section 271 threshold, a court or agency rules that NewCo's interest in Genuity results in a violation of section 271, NewCo's Class B shares shall be immediately convertible to the same extent as described above in section 2.B. In such event, NewCo shall be given a reasonable time extending beyond the date that such ruling becomes final and non-appealable in which to dispose of its Class B shares to the extent they are convertible into more than a 10% interest (or to convert those shares as part of a disposition), and may sell its shares to a third party subject to the limitation on sales proceeds described above.

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[2] Likewise, if, during such period, NewCo sells a portion of its stock but retains stock convertible into more than a 10% equity interest in Genuity, NewCo will have a right to retain only a prorated portion of the amount described in clause (ii) above; and if, during such period, NewCo sells all of its stock except for an amount convertible into less than a 10% equity interest, NewCo will have a right to retain the proceeds from the number of shares sold that, together with the number of shares retained, would be convertible into a 10% equity interest, plus the amount described in clause (ii) above.

3. Independence of Genuity

Until NewCo eliminates the applicable section 271 restrictions and exercises its option to take ownership of Genuity, Genuity will be independent of NewCo. Genuity will have an independent board of directors that is periodically elected by the voting shareholders consistent with the requirements of applicable corporation laws. Before the IPO, Genuity will elect six directors, including the CEO of Genuity, one director elected by a class vote of the Class B shares, and four independent directors who have no prior relationship with GTE or Bell Atlantic. Within 90 days following the IPO, the four independent directors will select seven additional directors who have no prior relationship with GTE or Bell Atlantic, which will bring the total board membership to 13 directors, a majority of whom will have been selected after the IPO. In addition, as soon as practicable, but in any event within nine months following the IPO, all directors except the Class B director will stand for election by the public shareholders. The Class B director will abstain from any vote before there are at least ten directors on the board and will at no time serve as chairman of the board. Exhibit B to the April 28, 2000 *ex parte* submission of William P. Barr describes more fully how the board of Genuity will be constituted and elected.

The board and officers of Genuity will owe fiduciary duties to the public shareholders. Incentive compensation for Genuity managers will be tied to the performance of Genuity and the value of Genuity's publicly traded stock, not to the financial performance or stock value of NewCo. The initial source of financing for Genuity will be the proceeds from the IPO of Class A stock. Any additional funding required by Genuity during the period before NewCo converts its Class B stock would be raised from the public markets, possibly by issuing additional Class A shares, by issuing debt to the public, or by arm's-length commercial loans. During such period, if NewCo were to choose to make loans to Genuity, NewCo could provide no more than 25% of the aggregate debt financing that Genuity is permitted to incur.

4. Investor Safeguards

NewCo's interests as a minority investor and potential future majority shareholder of Genuity will be protected by certain reasonable investor safeguards, which are described in Exhibit C to the April 28 *ex parte* submission of William P. Barr. NewCo's rights under these safeguards will remain in effect only until NewCo converts its Class B shares (or until NewCo no longer has a possibility of converting into more than a 10% interest). They are typical of the rights commonly held by prospective acquirers and are modeled on investor protections that have regularly been permitted by the Commission. These include the right to approve certain fundamental business changes that adversely impact the value of NewCo's minority investment and conversion rights, including a change in control of Genuity or the sale of a significant portion of its assets.

Genuity's business includes Internet backbone and related IP services. Genuity does not provide traditional switched voice long-distance service, and Genuity's business plan does not contemplate the acquisition of a traditional voice long-distance service provider. NewCo agrees not to consent, pursuant to any applicable investor safeguard rights, to Genuity's acquisition of a traditional voice long-distance provider unless the Commission has first reviewed and approved such acquisition.

5. Commercial Contracts Between NewCo and Genuity

Consistent with the fact that Genuity and NewCo will each be independent public corporations whose directors and officers will owe duties of care and loyalty to their respective shareholders, all commercial interactions between NewCo and Genuity will be pursuant to commercially reasonable contracts. (*See* "Commercial Contracts Between NewCo and DataCo," submitted for the record on April 3, 2000.)

Because a significant portion of Genuity's business will be outside the Bell Atlantic region or in in-region states where Bell Atlantic has eliminated applicable interLATA restrictions, NewCo will enter into a marketing agreement with Genuity for the period before NewCo exercises its conversion rights. (*See* "Purchase, Resale and Marketing Agreement," submitted as part of the "Commercial Contracts Between NewCo and DataCo.") Both GTE and Bell Atlantic are legally free to enter into this kind of commercial relationship today with a similarly situated company. Pursuant to this agreement, NewCo will market Genuity's services (or the two companies will market their services jointly) as and where permitted by law. For example, in New York, where Bell Atlantic has already received section 271 approval, NewCo and Genuity will jointly market Genuity's Internet connectivity services. The agreement provides that NewCo will not provide or jointly market any interLATA Genuity service in any state where NewCo does not have interLATA authority. The agreement is non-exclusive; either company may purchase from or sell to others. This marketing agreement will enable customers to begin realizing immediately some of the important Internet benefits promised by NewCo's eventual acquisition of Genuity and will also help to preserve Genuity's integrity and competitiveness until then.

NewCo and Genuity will also enter into certain additional commercial contracts, including contracts for transitional administrative support services to help ensure Genuity's stand-alone viability following the Genuity IPO. These transitional support contracts are typical of the commercially reasonable transitional arrangements that would be needed if Genuity were sold to a third party today. They will have a term of one year or less and will be terminable at any time by Genuity without penalty. In addition, these transitional services contracts may only be renewed by the parties if NewCo submits the contract in question to the Commission and provides 60-days advance notice to the Commission of the parties' intent to renew the contract and if, within such 60-day period, the Chief of the Common Carrier Bureau has not provided written notice to NewCo objecting to such renewal.

6. Independent Auditor

NewCo will hire an independent auditor, acceptable to the Chief of the Common Carrier Bureau, to monitor NewCo's ongoing compliance with the terms of this Revised Exhibit A.

REVISED EXHIBIT C

INVESTOR SAFEGUARDS

These investor safeguards shall be in effect only until NewCo converts its Class B shares:

- If at the time NewCo converts its shares, it owns shares at least equal to 70% of DataCo, it shall have the right to purchase from DataCo, at market, a number of shares that will increase its ownership to 80%.

- Class A shares initially contain a provision that: (i) prevents any single holder or group (as defined under SEC rules) from voting more than 20% of the Class A stock; and (ii) if any such person or group acquires over 20% of the Class A stock, the votes represented by the shares in excess of 20% shall be apportioned among the remaining Class A shareholders. This provision will expire upon conversion of a majority of the Class B shares.

- The Class B shareholders shall have the right to elect one member of the Board.

- Class vote of B shareholders required for:

    - Merger, consolidation, sale of all or substantially all assets or similar transactions;

    - Bankruptcy or liquidation;

    - Authorization of additional stock;

    - Amendments to Charter or certain By-law provisions that affect the rights of the Class B shareholders;

    - A material change in the nature or scope of DataCo's business; and

    - Any action that would make it unlawful for NewCo to exercise its conversion right.

- NewCo consent required for:

  - Agreements or arrangements that (i) bind or purport to bind NewCo or any of its affiliates or (ii) contain provisions that trigger a default, or provide for a material payment as a result of NewCo's exercise of its conversion right.

  - Declaration of extraordinary dividends or other extraordinary distributions.

  - Issuance of shares, securities convertible into shares or share equivalents ("Shares") except for: (i) Shares issued in connection with acquisitions provided that the aggregate number of Shares issued in connection with acquisitions does not exceed 30% of the shares outstanding at the close of DataCo's initial public offering; (ii) Shares issued to fund operating needs, provided that the aggregate number of Shares issued to fund operating needs does not exceed 5% of the shares outstanding at the close of DataCo's initial public offering; and (iii) Shares issued or granted to employees (including pursuant to benefit plans) provided that (w) the number of Shares issued or granted to individuals who are employees on the date of DataCo's initial public offering does not exceed in the aggregate 5% of the shares outstanding at the close of DataCo's initial public offering, (x) the number of Shares issued or granted to individuals who become employees of DataCo within nine months after its initial public offering, other than individuals who become employees as a result of their employer being acquired by DataCo ("Acquisition Employees"), does not exceed in the aggregate 1% of the shares outstanding at the close of DataCo's initial public offering, (y) the number of Shares issued or granted to individuals who become employees of DataCo beginning nine months after its initial public offering, other than Acquisition Employees, does not exceed in the aggregate 3% of the shares outstanding at the close of DataCo's initial public offering, and (z) the number of Shares issued or granted to Acquisition Employees does not exceed 6% multiplied by the total of (i) the number of shares outstanding at the close of DataCo's initial public offering, plus (ii) the number of Shares issued in connection with acquisitions completed by DataCo, minus (iii) the aggregate number of Shares that may be issued under clauses (w), (x) and (y) above.

  - An acquisition or a series of related acquisitions that equal more than 20% of the fair market value of DataCo's assets or an acquisition or joint venture that is in excess of $100 million and is not closely related to DataCo's business.

- A disposition or a series of related dispositions that are in excess of 20% of the fair market value of DataCo's assets.

- The incurrence of debt in excess of $11 billion over a five year period, provided that DataCo shall not be permitted to incur more than 35% of such debt in any single year.