

NEWMAN, COMLEY & RUTH

PROFESSIONAL CORPORATION

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June 19, 2000

FILED²

JUN 19 2000

Missouri Public
Service Commission
TA-2000-829

The Honorable Dale Hardy Roberts
Secretary/Chief Regulatory Law Judge
Missouri Public Service Commission
P.O. Box 360
Jefferson City, MO 65102-0360

Re: Cypress Communications Operating Company, Inc.; Basic Local Application

Dear Judge Roberts:

Enclosed for filing in the above-referenced matter, please find the original and eight copies of an Application for a Certificate of Service Authority to Provide Basic Local Telecommunications Services Throughout the State of Missouri and to Classify Said Services and the Company as Competitive. I note that I filed a motion for a protective order with the Commission in conjunction with a portion of Exhibit 2 of the Application and also enclose the original and eight copies of the highly confidential portion of Exhibit 2 which is filed under seal.

If you have any questions, please advise. Thank you very much for your attention to this matter.

Sincerely,

NEWMAN, COMLEY & RUTH, P.C.

By: *Cathleen A. Martin*

Cathleen A. Martin

martinc@ncrpc.com

CAM/slw

Enclosures

cc: Office of Public Counsel
General Counsel
Gregory Fickling

BEFORE THE PUBLIC SERVICE
COMMISSION OF THE STATE OF MISSOURI

FILED²
JUN 19 2000

Missouri Public
Service Commission

In the Matter of the Application of)

Cypress Communications Operating Company, Inc.)

for a Certificate of Service Authority to Provide)
Basic Local Telecommunications Services)
Throughout the State of Missouri and to Classify)
Said Services and the Company as Competitive)

Case No. TA-2000-829

**APPLICATION FOR A CERTIFICATE OF SERVICE AUTHORITY TO
PROVIDE BASIC LOCAL EXCHANGE TELECOMMUNICATIONS SERVICES
AND FOR COMPETITIVE CLASSIFICATION**

Comes now Cypress Communications Operating Company, Inc. ("Cypress" or "Applicant"), by its undersigned counsel, and hereby applies pursuant to Sections 392.361, 392.420, and 392.430 RSMo 1994, 392.410, 392.450 RSMo Supp. 1996, the Federal Telecommunications Act of 1996, and 4 CSR 240-2.060, for authority to provide basic local exchange telecommunications service in the State of Missouri and to classify said service as competitive. In support of its Application Cypress states as follows:

I. Applicant Information

1. Applicant's legal name is Cypress Communications Operating Company, Inc., a Delaware corporation. Applicant maintains its principal place of business at:

15 Piedmont Center, Suite 100
Atlanta, GA 30305
Tel.: (404) 869-2500
Fax: (404) 869-2525

2

2. Cypress' registered agent in Missouri is:

The Corporation Company
120 South Central Avenue
Clayton, MO 63105

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

Cathleen A. Martin
Newman, Comley & Ruth, P.C
601 Monroe Street, Suite 301
P. O. Box 537
Jefferson City, Missouri 65102-0537
Telephone: (573) 634-2266
Facsimile: (573) 636-3306

and

Russell M. Blau
Alexander M. Stokas
Swidler Berlin Shereff Friedman, LLP
3000 K Street, NW, Suite 300
Washington, D.C. 20007-5116
Tel.: (202) 424-7500
Fax: (202) 424-7645

with a copy to:

Robert W. McCarthy
Vice President, General Counsel, and Assistant Secretary
Cypress Communications Operating Company, Inc.
c/o Cypress Communications, Inc.
15 Piedmont Center, Suite 100
Atlanta, GA 30305
Tel.: (404) 869-2500
Fax: (404) 869-2525

4. Questions concerning the ongoing operations of Cypress following certification should be directed to:

Robert W. McCarthy
Vice President, General Counsel, and Assistant Secretary
Cypress Communications Operating Company, Inc.
c/o Cypress Communications, Inc.
15 Piedmont Center, Suite 100
Atlanta, GA 30305
Tel.: (404) 869-2500
Fax: (404) 869-2525

5. The following toll-free number is available for customer service inquiries: (877) 590-5955.

II. Requirements of 4 CSR 240-2.060(4)

Articles of Incorporation and Authorization to do Business in Missouri

1. Cypress, a Delaware corporation, is a wholly-owned subsidiary of Cypress Communications, Inc., a Delaware corporation. Cypress is qualified to do business in the State of Missouri. Copies of Cypress' Certificate of Incorporation and Certificate of Authority to Transact Business in the State of Missouri are attached hereto as Exhibit 1.

Description of Services

2. Cypress proposes to provide basic local exchange services, initially on a resale basis, to subscribers to and from all points in Missouri and, therefore, seeks statewide authorization. Cypress will resell the services of the underlying (competitive or incumbent) local exchange carrier(s) and plans to lease or purchase its own facilities in the future at which time it will resell unbundled network elements as well.
3. Initially, Cypress plans to offer the following categories of Local Exchange Access services to business customers located in multi-tenant environments in the State of Missouri:

- a. basic business lines;
- b. analog private branch exchange (PBX) trunks;
- c. analog direct inward dial (DID) trunks; and
- d. digital PBX and DID trunks.

Each of these services will provide dial tone access to the public switched telecommunications network and may be equipped with various features and functions.

4. Cypress also intends to offer the following Local Exchange Usage services to customers of its local exchange access services:

- a. direct dial calling;
- b. toll free calling (i.e., local 800, 950, or comparable services);
emergency 9-1-1 service, at no charge to the caller.

Cypress' basic local exchange services will be available 24 hours per day, 7 days per week.

Description of Exchanges where Applicant will offer Services

5. Applicant seeks authority to provide basic local exchange telecommunications services in all exchanges currently served by Southwestern Bell Telephone Company ("SWBT"), GTE Midwest, Inc. ("GTE") and Sprint/United Telephone Company ("Sprint"). The specific SWBT, GTE and Sprint exchanges within which Cypress proposes to offer service are listed in the incumbents' respective local exchange tariffs. Cypress seeks statewide authority so that it may expand its service areas as market conditions may warrant.

6. Pursuant to applicable law, and subject to Applicant's right under federal or state laws to seek to offer, and offer and provide service in geographical areas smaller than an exchange or in market segmentations or to offer customer specific pricing, similarly situated subscribers located within the listed exchanges will receive services on equal terms and conditions, as set forth in Applicant's tariffs.

Tariff Requirement

7. Cypress respectfully requests that the Commission grant Applicant a temporary waiver of 4 CSR 240-2.060(4)(H) with respect to its basic local telecommunications services tariff until Cypress has executed interconnection agreements with the underlying ILEC(s). Cypress cannot price its services until it has reached interconnection and/or resale agreements with the ILECs from which it will purchase those services. Once it is possible to do so, Cypress will submit to the Commission for approval a proposed basic local exchange tariff with a minimum 30 day effective date. Along with that filing Cypress will provide written disclosure of all interconnection agreements it has entered which affect its Missouri service areas.

III. Requirements of Section 392.455 RSMo Supp. 1996

Financial Qualifications

1. Cypress is financially qualified to provide basic local exchange telecommunications services in the State of Missouri. Specifically, Cypress has access to the financing and capital necessary to conduct its telecommunications operations as specified in this Application. Cypress will rely upon its existing personnel and technological and financial resources to provide the proposed telecommunications services, in addition to the resources available to the Applicant from its parent company. In support of Cypress' Application, attached hereto as Exhibit 2 are: (1) the Applicant's most recent financial statements; (2) a guaranty issued on behalf of the Applicant by its parent company, Cypress Communications, Inc. ("Cypress, Inc."); as well as (3) the most recent SEC Forms 10-K and 10-Q filed by Cypress, Inc. with the Securities and Exchange Commission. These latter two exhibits are offered to demonstrate that Cypress, through

its parent company Cypress, Inc., possesses sufficient capital to provide the proposed services in the State of Missouri.

Managerial and Technical Qualifications

2. Cypress has the managerial resources necessary to provide facilities-based and resold basic local exchange services throughout Missouri. Cypress' officers are well qualified to execute its business plan, to provide its proposed telecommunications services and to operate and maintain Cypress' facilities over which such services will be deployed. Brief descriptions of the telecommunications experience of Cypress' officers are attached hereto as Exhibit 3.

Commission Minimum Service Standards

3. Cypress' basic local telecommunications services will be equal to or superior to the quality of the basic local telecommunications services that customers in the State of Missouri are currently receiving from the incumbent providers. Cypress will meet all service standards applicable to telecommunications services, including but not limited to billing, quality of service, and the filing and maintenance of tariffs, except as waived by the Commission.

Separate and Distinct Service

4. Cypress will offer basic local telecommunications service as a separate and distinct service pursuant to Section 392.455(4) RSMo.

Equitable Access

5. Cypress will provide equitable access, as determined by the Commission for all Missourians within the geographic area in which it will offer basic local services in compliance with Section 392.455(5) RSMo. Supp. 1999.

IV. Classification as a Competitive Company

1. Cypress also seeks classification of itself and its services as competitive, with accompanying reduced regulation, pursuant to Section 392.361 RSMo. In determining the classification of an applicant, the Commission may consider such factors as market share, financial resources, and name recognition, among others. See In the Matter of the Investigation for the Purpose of Determining the Classification of the Services Provided by Interexchange Telecommunications Companies within the State of Missouri, 30 Mo. P.S.C. (N.S.) 16 (1989); In the Matter of Southwestern Bell Telephone Company's application for Classification of Certain Services as Transitionally Competitive, 1 Mo. P.S.C. 3d 479, 484 (1992). All the services a competitive company provides must be classified as competitive. Cypress submits that as a new market entrant, it does not have the market share or name recognition to inhibit competition. To the contrary, the Commission's approval of this Application will create competition for those ILECs that now possess sufficient market share and name recognition to dominate the telecommunications service market in the State of Missouri. Allowing Cypress to compete with existing ILECs, such as SWBT and GTE, will bring benefits such as lower costs and better service to residents of the State of Missouri. The public interest benefits of competition justify a lesser degree of regulation for carriers such as Cypress.

2. Cypress will comply with all applicable statutes and Commission rules, regulations, decisions, and orders governing the provision of Cypress' proposed services. Cypress, however, requests that, at a minimum, the following statutes and regulations be waived at this time consistent with the Commission's previous decisions regarding other telecommunications providers:

Statutes

Section	392.210.2	-	Uniform System of Accounts
Section	392.240(1)	-	setting just and reasonable rates
Section	392.270	-	valuation of property (rate making)
Section	392.280	-	depreciation accounts
Section	392.290.1	-	issuance of securities
Section	392.300.2	-	acquisition of stock
Section	392.310	-	stock and debt issuance
Section	392.320	-	stock dividend payment
Section	392.330	-	issuance of securities, debts and notes
Section	392.340	-	reorganization(s)

Commission Rules

4 CSR 240-10.020	-	depreciation fund income
4 CSR 240-30.010(2)(C)	-	posting of rate schedules at central offices
4 CSR 240-30.040	-	Uniform System of Accounts
4 CSR 240-32.030(4)(C)	-	filing of exchange boundary maps
4 CSR 240-33.030	-	Inform customers of lowest price available
4 CSR 240-35	-	reporting of bypass and customer specific arrangements

3. Cypress, consistent with Section 386.570 RSMo Cum. Supp. 1999, will comply with all applicable Commission rules except those which are specifically waived by the Commission pursuant to a request filed by the Cypress. To the extent that the Commission may modify its current waiver policies, Cypress respectfully reserves the right to amend its waiver requests accordingly.

V. PUBLIC INTEREST

1. Cypress submits that the public interest will be served by Commission approval of this application because Cypress' proposed services will create and enhance competition and expand customer service options consistent with the legislative goals set

forth in the Federal Telecommunications Act of 1996 and Chapter 392 RSMo. Prompt approval of this application also will expand the availability of innovative, high quality, and reliable telecommunications services within the State of Missouri.

WHEREFORE, Cypress Communications Operating Company, Inc., requests that the Missouri Public Service Commission grant it a Certificate of Service Authority to provide all forms of resold and facilities-based basic local telecommunications services, classify Applicant and its proposed services as competitive, and grant Cypress a waiver of the statutes and regulations referenced above.

Respectfully submitted,



Cathleen A. Martin #45682
Newman, Comley & Ruth, P.C
601 Monroe Street, Suite 301
P. O. Box 537
Jefferson City, Missouri 65102-0537
Telephone: (573) 634-2266
Facsimile: (573) 636-3306

Russell M. Blau
Swidler Berlin Shereff Friedman, LLP
3000 K Street, NW, Suite 300
Washington, D.C. 20007
Tel: (202) 424-7500
Fax: (202) 424-7645

Counsel for
Cypress Communications Operating
Company, Inc.

Dated: June 19, 2000

Certificate of Service

I hereby certify that a copy of this document has been hand delivered or mailed by first class mail, postage prepaid, to the Office of Public Counsel, on this 19th day of June, 2000.

Calvin A. Martin

EXHIBITS

Exhibit 1 Certificate of Incorporation and
Certificate of Authority to Transact Business

Exhibit 2 Financial Qualifications

- 1999 SEC Forms 10-K and 10-Q for Applicant's corporate parent, Cypress Communications, Inc.
- Financial Statements of Cypress Communications Operating Company, Inc. for the period ended April 30, 2000
(Filed Under Seal)
- Guaranty issued on behalf of Cypress Communications Operating Company, Inc. by Cypress Communications, Inc.

Exhibit 3 Managerial Qualifications

Affidavit

EXHIBIT 1

**Certificate of Incorporation
and
Certificate of Authority to Transact Business**

State of Delaware

PAGE 1

Office of the Secretary of State

I, EDWARD J. FREEL, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY THE ATTACHED IS A TRUE AND CORRECT COPY OF THE CERTIFICATE OF INCORPORATION OF "CYPRESS COMMUNICATIONS OPERATING COMPANY, INC.", FILED IN THIS OFFICE ON THE SIXTH DAY OF APRIL, A.D. 2000, AT 11:30 O'CLOCK A.M.

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




Edward J. Freel, Secretary of State

3207755 8100

001175593

AUTHENTICATION: 0367286

DATE: 04-07-00

CERTIFICATE OF INCORPORATION

OF

CYPRESS COMMUNICATIONS OPERATING COMPANY, INC.

1. The name of the corporation is Cypress Communications Operating Company, Inc.
2. The address of its registered office in the State of Delaware is Corporation Trust Center, 1209 Orange Street, in the City of Wilmington, County of New Castle. The name of its registered agent at such address is The Corporation Trust Company.
3. The purpose of the corporation is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of Delaware.
4. The total number of shares of stock which the corporation shall have authority to issue is 1,000 shares of Common Stock. The par value of each of share is \$01.
5. The name and mailing address of the incorporator is as follows:

Name	Mailing Address
Michael S. Turner	Goodwin, Procter & Hoar LLP Exchange Place Boston, MA 02109

The powers of the incorporator shall terminate upon the filing of this Certificate of Incorporation.

6. The name and mailing address of each person who is to serve as a director until the first annual meeting of the stockholders or until a successor is elected and qualified, is as follows:

Name	Mailing Address
R. Stanley Allen	c/o Cypress Communications, Inc. Fifteen Piedmont Center Suite 710 Atlanta, GA 30305

APR-11-00 10:34 From: GOODWIN, PROCTER & HOAR LLP
AFR-08-00 10:34 FROM: GOODWIN, PROCTER & HOAR LLP+6175708150 T-708 P.05/08 Job-913
0110100100

Mark A. Graves

c/o Cypress Communications, Inc.
Fifteen Piedmont Center
Suite 710
Atlanta, GA 30305

Barry L. Boniface

c/o Cypress Communications, Inc.
Fifteen Piedmont Center
Suite 710
Atlanta, GA 30305

7. In furtherance and not in limitation of the powers conferred by statute, the Board of Directors is expressly authorized to adopt, amend or repeal the by-laws of the corporation.

8. Elections of directors need not be by written ballot unless the by-laws of the corporation shall so provide.

9. A director of the corporation shall not be personally liable to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director except for liability (i) for any breach of the director's duty of loyalty to the corporation or its stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) under Section 174 of the Delaware General Corporation Law, or (iv) for any transaction from which the director derived any improper personal benefit. No amendment or repeal of this Section shall adversely affect the rights and protection afforded to a director of the corporation under this Section for acts or omissions occurring prior to such amendment or repeal.

10. No action on a matter to be taken by stockholders without a meeting under Section 228 of the Delaware General Corporation Law may be taken without the written consent of the holders of all of the outstanding stock entitled to vote on the matter.

11. The corporation reserves the right to amend, alter, change or repeal any provision contained in this Certificate of Incorporation, in the manner now or hereafter prescribed by statute, and all rights conferred upon stockholders herein are granted subject to this reservation.

APR-11-00 10:34 From:GOODWIN, P. & HOAR LLP
APR-06-00 10:20 From:GOODWIN, PHILIP & HOAR LLP

+8175708150
DISTRIBUTION

T-708 P.06/06 Job-913

THE UNDERSIGNED incorporator, for the purpose of forming a corporation pursuant to the General Corporation Law of the State of Delaware, does hereby make this certificate, hereby declaring and certifying that it is his free act and deed and the facts herein stated are true, and accordingly he has hereunto set his hand this 6th day of April, 2000.

Michael S. Turner

Michael S. Turner, Incorporator

DOCS\867242.1

No. F00482663

STATE OF MISSOURI



Rebecca McDowell Cook
Secretary of State

CORPORATION DIVISION - CERTIFICATE OF AUTHORITY

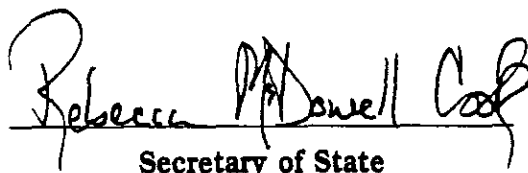
WHEREAS,
CYPRESS COMMUNICATIONS OPERATING COMPANY, INC.

using in Missouri the name
CYPRESS COMMUNICATIONS OPERATING COMPANY, INC.

has complied with the General and Business Corporation Law which governs Foreign Corporations; by filing in the office of the Secretary of State of Missouri authenticated evidence of its incorporation and good standing under the Laws of the State of DELAWARE.

NOW, THEREFORE, I, REBECCA McDOWELL COOK, Secretary of State of the State of Missouri, do hereby certify that said corporation is from this date duly authorized to transact business in this State, and is entitled to all rights and privileges granted to Foreign Corporations under the General and Business Corporation Law of Missouri.

IN TESTIMONY WHEREOF, I have set my hand and imprinted the GREAT SEAL of the State of Missouri, on this, the 20th day of APRIL, 2000.


Secretary of State

\$155.00





State of Missouri

Rebecca McDowell Cook, Secretary of State

P.O. Box 778, Jefferson City, Mo. 65102
Corporation Division

FILED
AND CERTIFICATE OF
AUTHORITY ISSUED

APR 20 2000

**Application for Foreign Corporation
for a Certificate of Authority**

(Submit in duplicate with filing fee of \$155.00)

Rebecca McDowell Cook
SECRETARY OF STATE

- (1) The corporation's name is Cypress Communications Operating Company, Inc.
and it is organized and existing under the laws of Delaware
- (2) The name it will use in Missouri is Cypress Communications Operating Company, Inc.
- (3) The date of its incorporation was April 6, 2000, (month/day/year),
and the period of its duration is perpetual
- (4) The address of its principal place of business (Address/City/State/Zip)
15 Piedmont Center, Suite 710, Atlanta, GA 30305
- (5) The name and address of its registered agent and office in the State of
Missouri is (Name, Address, City/State/Zip)
C T CORPORATION SYSTEM, 120 South Central Avenue, Clayton, Missouri 63105
- (6) The specific purpose(s) of its business in Missouri are: to be a comprehensive
local exchange carrier.
- (7) The name of its officers and directors and their business addresses are as
follows:
- Officers** (Name/Address/City/State/Zip)
- President Please see Attachment A
- Vice President _____
- Secretary _____

Treasurer _____

Board of Directors (Name/Address/City/State/Zip)

Director _____ Please see Attachment A

Director _____

Director _____

Director _____

(8) The effective date of this document is the date it is filed by the Secretary of State of Missouri, unless you indicate a future date, as follows:

(Date may not be more than 90 days after the filing date in this office)

In affirmation thereof, the facts stated above are true.

Robert W. McCarthy

April 18, 2000

(Authorized signature of officer or chairman of the board) (Title) (Date)

Robert W. McCarthy, Vice President, General Counsel and Assistant Secretary

Note: You must have a current certificate of good standing or certificate of existence with this application. This may be obtained from the Secretary of State or other authority that issues corporate charters.

FILED
AND CERTIFICATE OF
THAT THE STATE

APR 20 2000

Rebecca McDowell Cook
SECRETARY OF STATE

Attachment A

The names and usual business addresses of the current directors of Cypress Communications Operating Company, Inc. are:

<u>Name</u>	<u>Address</u>
R. Stanley Allen	c/o Cypress Communications, Inc. Fifteen Piedmont Center, Suite 710 Atlanta, GA 30305
Mark A. Graves	c/o Cypress Communications, Inc. Fifteen Piedmont Center, Suite 710 Atlanta, GA 30305
Barry L. Boniface	c/o Cypress Communications, Inc. Fifteen Piedmont Center, Suite 710 Atlanta, GA 30305

The names and usual business addresses of the current officers of Cypress Communications Operating Company, Inc. are:

<u>Name</u>	<u>Title</u>	<u>Address</u>
R. Stanley Allen	CEO	c/o Cypress Communications, Inc. Fifteen Piedmont Center, Suite 710 Atlanta, GA 30305
Mark A. Graves	President, COO and Secretary	c/o Cypress Communications, Inc. Fifteen Piedmont Center, Suite 710 Atlanta, GA 30305
Barry L. Boniface	CFO, VP and Treasurer	c/o Cypress Communications, Inc. Fifteen Piedmont Center, Suite 710 Atlanta, GA 30305
Ward C. Bourdeaux, Jr.	Executive VP	c/o Cypress Communications, Inc. Fifteen Piedmont Center, Suite 710 Atlanta, GA 30305
Robert W. McCarthy	VP, General Counsel and Asst. Secretary	c/o Cypress Communications, Inc. Fifteen Piedmont Center, Suite 710 Atlanta, GA 30305

EXHIBIT 2

Financial Qualifications

1999 SEC Forms 10-K and 10-Q for
Applicant's corporate parent, Cypress Communications, Inc.

Financial Statements of Cypress Communications Operating Company, Inc.
for the period ended April 30, 2000
(Filed Under Seal)

Guaranty issued on behalf of Cypress Communications Operating Company, Inc.
by Cypress Communications, Inc.

CYPRESS COMMUNICATIONS, INC.
BALANCE SHEETS
DECEMBER 31, 1998 AND 1999

ASSETS

	1998	1999
CURRENT ASSETS:		
Cash and cash equivalents	\$11,057,696	\$69,475,288
Accounts receivable, net of allowance for doubtful accounts of \$79,520, and \$367,805 in 1998 and 1999, respectively	1,119,784	1,665,203
Note receivable	200,000	0
Prepaid expenses and other	26,238	320,516
Total current assets	12,403,718	71,461,007
PROPERTY AND EQUIPMENT, net	6,291,413	27,028,102
OTHER ASSETS:		
Cost in excess of net assets acquired, net of accumulated amortization of \$7,071 and \$15,556 in 1998 and 1999, respectively	84,141	75,656
Tenant contracts, net of accumulated amortization of \$119,444 and \$262,778 in 1998 and 1999, respectively	418,056	274,722
License agreements	0	23,398,094
Other	209,777	617,020
Total other assets	711,974	24,365,492
Total assets	\$19,407,105	\$122,854,601

LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY

CURRENT LIABILITIES:		
Accounts payable	\$381,032	\$12,672,121
Accrued expenses	1,307,941	2,696,133
Current portion of capital lease obligations	192,635	217,468
Total current liabilities	1,881,608	15,585,722
LONG-TERM PORTION OF CAPITAL LEASE OBLIGATIONS	522,583	283,469
Total liabilities	2,404,191	15,869,191
CONVERTIBLE REDEEMABLE PREFERRED STOCK (Note 5):		
\$.001 par value; 1,211,140 shares designated Series A in 1998 and 1999; 1,211,140, shares issued and outstanding in 1998 and 1999, entitled to redemption value of \$5 per share	6,036,670	6,040,856
\$.001 par value; 1,912,813 and 1,919,188 shares designated Series B in 1998 and 1999, respectively; 1,333,200 and 1,339,575 shares issued and outstanding in 1998 and 1999, respectively, entitled to redemption value of \$8 per share	10,650,328	10,705,636
\$.001 par value; 579,613 shares designated Series B-1 in 1998 and 1999; 579,613 shares issued and outstanding in 1998 and 1999, entitled to redemption value of \$8 per share	4,630,265	4,632,137
\$.001 par value; 0 and 4,210,526 shares designated Series C in 1998 and 1999, respectively; 0 and 4,161,974 shares issued and outstanding in 1998 and 1999, respectively, entitled to redemption value of \$19 per share	0	78,899,121
Total preferred stock	21,317,263	100,277,750
COMMITMENTS AND CONTINGENCIES (Note 7)		
STOCKHOLDERS' (DEFICIT) EQUITY:		
Common stock, \$.001 par value; 20,594,088 and 58,620,758 shares authorized in 1998 and 1999, respectively; 2,636,906 and 2,759,806 shares issued and outstanding in 1998 and 1999, respectively	2,637	2,760
Additional paid-in capital	3,536,863	109,339,640
Warrants outstanding	0	23,398,094
Deferred compensation	(2,179,045)	(27,124,250)
Accumulated deficit	(5,674,804)	(98,908,584)
Total stockholders' (deficit) equity	(4,314,349)	6,707,660
Total liabilities and stockholders' deficit	\$19,407,105	\$122,854,601

The accompanying notes are an integral part of these balance sheets.

CYPRESS COMMUNICATIONS, INC.

STATEMENTS OF OPERATIONS

For the years ended December 31, 1997, 1998, and 1999

	<u>1997</u>	<u>1998</u>	<u>1999</u>
REVENUES	<u>\$709,402</u>	<u>\$2,417,816</u>	<u>\$7,437,496</u>
OPERATING EXPENSES:			
Cost of services	603,114	1,539,846	4,966,851
Sales and marketing, including noncash compensation expense of \$0, \$19,248, and \$321,492 in 1997, 1998, and 1999, respectively	448,916	1,489,355	4,007,094
General and administrative, including noncash compensation expense of \$0, \$98,345, and \$1,403,796 in 1997, 1998, and 1999, respectively	900,595	2,534,566	11,232,045
Depreciation and amortization	<u>196,415</u>	<u>576,659</u>	<u>2,197,831</u>
Total operating expenses	<u>2,149,040</u>	<u>6,140,426</u>	<u>22,403,821</u>
OPERATING LOSS	<u>(1,439,638)</u>	<u>(3,722,610)</u>	<u>(14,966,325)</u>
INTEREST INCOME, net	<u>113,922</u>	<u>232,279</u>	<u>810,045</u>
LOSS BEFORE INCOME TAXES	<u>(1,325,716)</u>	<u>(3,490,331)</u>	<u>(14,156,280)</u>
INCOME TAX BENEFIT	<u>0</u>	<u>0</u>	<u>0</u>
NET LOSS	<u>(1,325,716)</u>	<u>(3,490,331)</u>	<u>(14,156,280)</u>
BENEFICIAL CONVERSION FEATURE OF PREFERRED STOCK (Note 5)	<u>0</u>	<u>0</u>	<u>(79,077,500)</u>
NET LOSS AVAILABLE TO COMMON STOCKHOLDERS	<u>\$(1,325,716)</u>	<u>\$(3,490,331)</u>	<u>\$(93,233,780)</u>
NET LOSS PER COMMON SHARE:			
Basic and diluted	<u>\$(0.41)</u>	<u>\$(1.32)</u>	<u>\$(35.22)</u>
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING:			
Basic and diluted	<u>3,266,237</u>	<u>2,636,906</u>	<u>2,647,274</u>

The accompanying notes are an integral part of these statements.

CYPRESS COMMUNICATIONS, INC.

STATEMENTS OF MEMBERS' OR STOCKHOLDERS' DEFICIT

FOR THE YEARS ENDED DECEMBER 31, 1997, 1998, AND 1999

	Members' Shares or Common Stock		Contributed or Additional Paid-In Capital	Deferred Compensation	Warrants Outstanding	Accumulated Deficit	Total
	Shares	Amount					
BALANCE, December 31, 1996	400,431	\$ 0	\$ 1,887,513	\$ 0	\$ 0	\$ (858,757)	\$ 1,028,756
Issuance of member shares	41,667	0	250,000	0	0	0	250,000
Repurchase of member shares	(149,109)	0	(894,651)	0	0	0	(894,651)
Conversion to a C corporation	2,343,917	2,637	(2,637)	0	0	0	0
Net loss	0	0	0	0	0	(1,325,716)	(1,325,716)
BALANCE, December 31, 1997	2,636,906	2,637	1,240,225	0	0	(2,184,473)	(941,611)
Deferred compensation	0	0	2,296,638	(2,296,638)	0	0	0
Amortization of deferred compensation	0	0	0	117,593	0	0	117,593
Net loss	0	0	0	0	0	(3,490,331)	(3,490,331)
BALANCE, December 31, 1998	2,636,906	2,637	3,536,863	(2,179,045)	0	(5,674,804)	(4,314,349)
Issuance of common stock	122,900	123	395,127	0	0	0	395,250
Deferred compensation	0	0	26,330,150	(26,330,150)	0	0	0
Amortization of deferred compensation	0	0	0	1,384,945	0	0	1,384,945
Issuance of warrants	0	0	0	0	23,398,094	0	23,398,094
Beneficial conversion feature of preferred stock (Note 5)	0	0	79,077,500	0	0	(79,077,500)	0
Net loss	0	0	0	0	0	(14,156,280)	(14,156,280)
BALANCE, December 31, 1999	<u>2,759,806</u>	<u>\$ 2,760</u>	<u>\$ 109,339,640</u>	<u>\$(27,124,250)</u>	<u>\$ 23,398,094</u>	<u>\$(98,908,584)</u>	<u>\$ 6,707,660</u>

The accompanying notes are an integral part of these statements

CYPRESS COMMUNICATIONS, INC.

STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 1997, 1998, AND 1999

	<u>1997</u>	<u>1998</u>	<u>1999</u>
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net loss	\$ (1,325,716)	\$ (3,490,331)	\$ (14,156,280)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	196,415	576,650	2,197,831
Amortization of deferred compensation	0	117,593	1,384,945
Other	1,920	5,737	14,544
Noncash consulting expense	0	0	340,343
Changes in operating assets and liabilities:			
Accounts receivable, net	(168,919)	(916,616)	(545,419)
Prepaid expenses and other current assets	(32,146)	18,185	(294,278)
Other assets	0	(89,777)	(196,286)
Accounts payable and accrued expenses	436,927	863,645	1,353,953
Net cash used in operating activities	<u>(891,519)</u>	<u>(2,914,905)</u>	<u>(9,900,647)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchases of property and equipment	(1,190,723)	(2,887,243)	(10,365,122)
Purchase of assets of MTS Communications	0	(1,904,398)	0
(Advance to) repayment from MTS Communications	0	(200,000)	200,000
Other	0	0	19,400
Net cash used in investing activities	<u>(1,190,723)</u>	<u>(4,991,641)</u>	<u>(10,145,722)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:			
Proceeds from issuance of Series A preferred stock, net of offering expenses	5,975,560	55,000	0
Proceeds from issuance of Series B and B-1 preferred stock, net of offering expenses	0	15,279,046	51,000
Proceeds from issuance of Series C preferred stock, net of offering expenses	0	0	78,894,943
Proceeds from sale of member shares	250,000	0	0
Proceeds from exercise of stock options	0	0	54,907
Principal payments on capital lease obligations	(25,328)	(40,869)	(214,281)
Borrowings under line of credit	0	500,000	0
Repayments of line of credit	0	(500,000)	0
Acquisition of member interest	(894,651)	0	0
Payment of offering costs	0	0	(322,608)
Net cash provided by financing activities	<u>5,305,581</u>	<u>15,293,177</u>	<u>78,463,961</u>
INCREASE IN CASH AND CASH EQUIVALENTS	<u>3,223,339</u>	<u>7,386,631</u>	<u>58,417,592</u>
CASH AND CASH EQUIVALENTS, beginning of year	447,726	3,671,065	11,057,696
CASH AND CASH EQUIVALENTS, end of year	<u>\$ 3,671,065</u>	<u>\$11,057,696</u>	<u>\$ 69,475,288</u>
SUPPLEMENTAL DISCLOSURES:			
Cash paid for interest	<u>\$ 2,031</u>	<u>\$ 12,563</u>	<u>\$ 13,151</u>
Assets acquired under capital leases	<u>\$ 0</u>	<u>\$ 670,450</u>	<u>\$ 0</u>

The accompanying notes are an integral part of these statements.

CYPRESS COMMUNICATIONS, INC.

NOTES TO FINANCIAL STATEMENTS

DECEMBER 31, 1997, 1998, and 1999

1. Organization And Nature Of Business

Cypress Communications, Inc. (the "Company") was incorporated July 15, 1997 under the laws of Delaware. The Company was formed to effect the conversion of Cypress Communications, L.L.C. (the "Predecessor Company") to a C corporation. To effect this change in legal entity status, on July 15, 1997, the Predecessor Company was acquired by the Company and ceased to exist as a legal entity. The accompanying financial statements reflect this as a reorganization (the "Reorganization").

The Predecessor Company was incorporated August 16, 1995 as a limited liability company under the laws of Georgia. All references to the Company refer to both the Company and the Predecessor Company unless otherwise noted.

The Company provides a full range of communications services to small- and medium-sized businesses located in multi-tenant office buildings in major metropolitan markets in the United States. Since the inception of our Predecessor Company in August 1995, our principal activities have included securing license agreements with building owners and real estate managers that enable us to install our in-building fiber-optic, digital, and broadband networks, marketing our services to tenants, and hiring qualified personnel to support our rapid growth.

The Company has experienced operating losses since its inception. The Company expects to continue to focus on increasing its customer base and expanding its operations. Accordingly, the Company expects that its operating expenses and capital expenditures will continue to increase significantly, which will have a negative impact on short-term operating results and will require significant capital. Accordingly, the Company may be required to raise additional funds through public or private financing or other arrangements, or it may have to slow its rate of expansion. There can be no assurance that any required additional funding, if needed, will be available on terms attractive to the Company or at all, which could have a material adverse effect on the Company's business, financial condition, cash flows, and results of operations.

Other Risk Factors

The Company faces certain other risk factors including the following: growth and expansion may strain the Company's resources, dependence on key personnel, dependence on third-party suppliers of equipment and communications services, dependence on relationships with certain property owners or operators, competition from other providers of communications services, and potential disruption of services due to system failures.

2. Summary Of Significant Accounting Policies

Basis of Presentation

The accompanying financial statements are presented on the accrual basis of accounting using accounting principals generally accepted in the United States.

Accounting Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual amounts could differ from these estimates and such differences could be material.

Revenue Recognition

The Company's revenues include recurring charges for local access, long-distance, equipment rental, Internet, voicemail, inbound 800 charges, and other enhanced voice and data services as well as nonrecurring revenues for installations and moves, adds, and changes charges, all of which are recognized as services are provided. To date, nonrecurring revenues have not exceeded the related direct costs of installation in any significant amounts. All expenses related to services provided are recognized as incurred.

The Securities and Exchange Commission has released Staff Accounting Bulletin ("SAB") No. 101, "Revenue Recognition in Financial Statements." The Company is reviewing its policies with respect to SAB No. 101 and does not expect the impact of adoption to be material.

Cash and Cash Equivalents

The Company considers all highly liquid instruments with an original maturity of three months or less to be cash equivalents.

Property and Equipment

Property and equipment are stated at cost, and depreciation is computed using the straight-line method over the estimated useful lives of the assets (generally three to seven years). Leasehold improvements are depreciated over the lesser of the average lease term (or the term of the related license agreement) or the assets' useful lives. Depreciation expense was \$112,431, \$546,521, and \$1,953,761 for the years ended December 31, 1997, 1998, and 1999, respectively. Maintenance and repairs are charged to expense as incurred. Gains or losses on disposal of property and equipment are recognized in operations in the year of disposition. There were no significant gains or losses in any periods presented.

Income Taxes

The Predecessor Company was a limited liability company for federal and state income tax purposes. The Internal Revenue Code and applicable state statutes provide that income and expenses are not separately taxable to the limited liability company but rather accrue directly to the members. Subsequent to the Reorganization, income taxes have been provided for using the liability method in accordance with Statement of Financial Accounting Standards ("SFAS") No. 109, "Accounting for Income Taxes," (Note 8).

Intangibles

The cost over the fair values of net assets acquired was recorded in connection with the Company's purchase of substantially all of the assets of MTS Communications Company, Inc. ("MTS Communications") (Note 9). These costs are being amortized using the straight-line method over ten years. Tenant contracts were acquired in the MTS Communications acquisition and are being amortized using the straight-line method over three years.

Impairment of Long-Lived Assets

The Company reviews its long-lived assets, including property and equipment and intangibles, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset should be assessed. An impairment will be recognized when the undiscounted future net cash flows estimated to be generated by the asset are insufficient to recover the current carrying value of the asset. Estimates of future cash flows are based on many factors, including current operating results, expected market trends, and competitive influences. Management believes that the long-lived assets in the accompanying financial statements are appropriately valued.

Fair Value of Financial Instruments

The carrying amounts reported in the balance sheets approximate the fair values for cash and capital lease obligations.

In accordance with SFAS No. 107, "Disclosures about Fair Values of Financial Instruments," the Company has estimated the fair value of the Series A preferred stock as approximately \$5.8 million and \$81.8 million at December 31, 1998 and 1999, respectively. The Company has estimated the fair value of the Series B and Series B-1 preferred stock as \$6.4 million and \$2.8 million, respectively, at December 31, 1998 and approximately \$90.4 million and \$39.1 million, respectively, at December 31, 1999. The Series C preferred stock has an estimated fair value of approximately \$281 million at December 31, 1999. The fair value of the preferred stock is based on the estimated fair value of the Company's common stock and the number of shares of common stock upon conversion.

Segment Reporting

The Company reports one segment, communication services, and provides an integrated package of communication products to small- and medium-sized businesses.

Accrued Expenses

Accrued expenses relate to the following at December 31:

	1998	1999
Property and equipment additions	\$ 280,900	\$ 16,969
Compensation	257,838	1,116,873
Taxes	171,118	453,578
Network costs	221,912	422,366
Other	376,173	686,347
	<u>\$ 1,307,941</u>	<u>\$2,696,133</u>

Net Loss Per Common Share

Basic and diluted net loss per share is computed using the weighted average number of shares of common stock outstanding during the year. Potential common stock equivalents are excluded from the calculation of diluted net loss per share, as their effect is antidilutive. Convertible redeemable preferred stock was outstanding at December 31, 1997, 1998, and 1999. These securities were not considered in the computation of net loss per share as the conversion is dependent upon a qualifying public offering, as defined in the preferred stock sale agreements (Note 10).

3. Property And Equipment

Property and equipment consist of the following at December 31:

	<u>1998</u>	<u>1999</u>
System infrastructure	\$4,771,675	\$10,714,590
System equipment	1,583,018	4,136,654
Computer and office equipment	495,737	2,087,051
Leasehold improvements	220,655	989,075
Assets under construction	0	11,834,175
	<u>7,071,085</u>	<u>29,761,545</u>
Less accumulated depreciation and amortization	<u>(779,672)</u>	<u>(2,733,443)</u>
	<u>\$6,291,413</u>	<u>\$27,028,102</u>

4. Capital Transactions

Stock Option Plans

In February 1996, the Predecessor Company adopted the 1996 Share Incentive Plan (the "Predecessor Plan"). The Predecessor Plan was intended to provide incentives to officers and key employees of the Predecessor Company.

In July 1997, the 1997 Management Option Plan (the "1997 Option Plan") was adopted by the Company. The 1997 Option Plan provides for the granting of either incentive stock options or nonqualified stock options to purchase shares of the Company's common stock to officers, directors, and key employees responsible for the direction and management of the Company. The options expire ten years after the date of grant and vest 20% upon the first anniversary of the date of grant and 5% each subsequent quarter measured from the first anniversary of the date of grant.

On December 21, 1999, the Company's board of directors adopted the 2000 Stock Option Plan (the "2000 Plan") which was approved subsequently by the stockholders on December 23, 1999. All officers, directors, and key persons are eligible to participate in the plan, subject to the discretion of a committee appointed by the board of directors. The board of directors reserved a combined 11.7 million shares for issuance under the 1997 Option Plan and the 2000 Plan.

Statement of Financial Accounting Standards No. 123

A summary of the activity related to the option plans is as follows:

	Weighted Average Shares	Weighted Average Exercise Price
Balance at December 31, 1996	225,000	\$0.60
Forfeited	(45,000)	0.56
Granted	1,536,345	0.67
Balance at December 31, 1997	1,716,345	0.66
Granted	1,087,875	1.00
Forfeited	(76,500)	1.07
Balance at December 31, 1998	2,727,720	0.78
Granted	3,526,655	2.29
Forfeited	(310,500)	1.15
Exercised	(122,900)	0.94
Balance at December 31, 1999	5,820,975	1.64

In December 1999, the Company granted 25,655 options to purchase common stock, with an exercise price of \$2.53 per share, to consultants for prior services. The options vested immediately and the consultants exercised these options prior to December 31, 1999. The Company recorded an expense of approximately \$340,000 related to this grant.

The following table summarizes information about the stock options outstanding at December 31, 1999:

Exercise Price	Number of Options Outstanding at December 31, 1999	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Exercisable as of December 1999
\$0.67	1,808,100	7.66	\$0.67	876,132
\$1.07	2,149,875	9.20	1.07	172,959
\$2.53	1,773,000	9.90	2.53	0
\$17.00	90,000	9.95	17.00	0
\$0.67-\$17.00	5,820,975	8.95	1.64	1,049,091

The Company applies Accounting Principles Board Opinion No. 25 and related interpretations in accounting for its option plans. The Company recorded deferred compensation of approximately \$2.3 million in 1998 and \$26.3 million in 1999 which represents the difference between the exercise price per option and the fair value of the Company's common stock at the dates of grant. Deferred compensation is amortized over the vesting period of the stock options which is generally five years.

Had compensation cost for the Company's stock-based compensation plans been determined consistent with SFAS No. 123, the Company's net loss would have been the pro forma amounts indicated below. The pro forma net loss is calculated using the Black-Scholes option pricing model, with the following assumptions: risk-free interest rates from 5.82% to 6.19% for 1997, 5.28% for 1998, and 6.05% for 1999, expected life of 6 years for 1997 and 1998, and 3 1/2 years for 1999, dividend yield of 0%, and expected volatility of 0% for all periods prior to the Company's filing for an initial public offering and 65% for

December 4, 1999 through December 31, 1999. The weighted average fair value of options granted during the years ended December 31, 1997, 1998, and 1999 was \$.18, \$.22, and \$40.80 per option, respectively.

	Year Ended December 31		
	1997	1998	1999
Net loss, as reported	\$ (1,325,716)	\$ (3,490,331)	\$ (93,233,780)
Net loss, pro forma	(1,375,439)	(3,538,833)	(93,354,915)
Net loss per common share, as reported	\$(0.41)	\$(1.32)	\$(35.22)
Net loss per common share, pro forma	(0.42)	(1.34)	(35.26)

Shareholder Rights Plan

In December 1999, the Company approved a stockholder rights plan. This plan entitles the stockholders to rights to acquire additional shares of the Company's common stock when a third party acquires 15% of the Company's common stock or commences or announces its intent to commence a tender offer for at least 15% of the Company's common stock. This plan could delay, deter, or prevent a change of control.

Employee Stock Purchase Plan

In December 1999, the board of directors and stockholders approved an employee stock purchase plan. Up to 900,000 shares of common stock may be issued under this plan.

Amendment to Certificate of Incorporation

In September 1998, the Company amended and restated its certificate of incorporation (the "Certificate") to, among other things, increase the total number of authorized common stock and preferred stock to 20,594,088 and 3,703,566, respectively. Additionally, the Certificate amended the terms of the existing Series A preferred stock and increased the number of shares of preferred stock designated as Series A to 1,211,140.

In October 1999, the Company increased the authorized number of shares of its common stock and preferred stock to 49,023,324 and 7,687,704, respectively. In October 1999, the Company designated an additional 6,375 shares as Series B preferred stock and designated 3,977,763 shares as Series C preferred stock. In December 1999, the Company increased the authorized number of its common stock and preferred stock to 58,620,758 and 7,920,467, respectively, and designated an additional 232,763 shares as Series C preferred stock.

Stock Split

In May 1998, the Company's board of directors and the majority stockholders approved a 2-for-1 stock split (the "Split") with respect to each outstanding share of common stock and Series A preferred stock. The Split was effected in the form of a stock dividend that was paid in September 1998. All references to common stock and Series A share amounts have been restated to reflect the Split on a retroactive basis. See Note 10 regarding a stock split in February 2000.

Warrants

In November and December 1999, the Company entered into master license agreements and stock warrant agreements with several property owners and operators. Under the terms of these agreements, the Company issued warrants to purchase up to an aggregate of approximately 11 million shares of the Company's common stock at an exercise price of \$4.22 per share. These warrants are exercisable for periods of five to ten

years. The exact number of shares of common stock underlying the warrants, which is based on the gross leaseable area of the building set forth in the master license agreements, will be determined upon the completion of a due diligence period and the finalization of the building schedules, which is expected to be complete in April 2000. The measurement date for valuing the warrants will be the date(s) upon which the property owners or operators effectively complete their performance requirements. Such amounts will be recorded as deferred license inducement expense, and will be amortized over the terms of the related license agreements, which are expected to be ten years.

5. Convertible Redeemable Preferred Stock

Sales of Preferred Stock

On July 15, 1997, the Company issued 1,200,140 shares of its Series A preferred stock for \$5 per share. On September 30, 1998, the Company issued 1,333,200 and 579,613 shares of its Series B and Series B-1 preferred stock, respectively, for \$8 per share. In October 1999, in connection with the second amended and restated stockholders' agreement, certain terms of the Series A, Series B, and Series B-1 preferred stock were changed.

In February 1999, the Company issued 6,375 shares of its Series B preferred stock to two employees of the Company for \$8 per share for total proceeds of \$51,000.

In October 1999, the Company issued 2,819,868 shares of its Series C preferred stock to existing and new third-party investors for \$19 per share for total proceeds of approximately \$53.6 million.

In November 1999 and December 1999, the Company issued 1,157,895 and 184,211 shares, respectively, of its Series C preferred stock to certain property owners and operators for \$19 per share for total proceeds of \$25.5 million.

Terms of Preferred Stock

The Series A, Series B and B-1, and Series C preferred stock (the "Preferred Stock") have a redemption price of \$5, \$8, and \$19 per share, respectively, together with accrued and unpaid dividends thereon. Redemption is mandatory beginning October 8, 2005, at which time up to one-third of the outstanding shares may be redeemed on October 8, 2005, October 8, 2006, and October 8, 2007. In the event of any liquidation, dissolution, or winding up of the affairs of the Company, holders of Series C preferred stock shall be paid the redemption price, plus all accrued dividends, before any payment to other stockholders. Holders of Series B and Series B-1 preferred stock shall be paid the redemption price, plus all accrued dividends, before any payment to other stockholders, exclusive of any payments to be made to the holders of the Series C preferred stock. Holders of Series A preferred stock shall be paid the redemption price, plus all accrued dividends, before any payment to other stockholders, exclusive of any payments to be made to holders of Series B and Series B-1 and Series C preferred stock. The Preferred Stock is convertible into common stock at the discretion of the holder and automatically converts into common stock upon the completion of an initial public offering of the Company's common stock with proceeds in excess of \$50,000,000 and an adjusted per share price of at least \$8.44. These shares are entitled to 4.5 votes per share on all matters upon which common stockholders are entitled to vote, except for the Series B-1 shares which do not have any voting rights. Under these conversion terms, the Preferred Stock converts 4.5 for 1 into common stock. The holders of the Preferred Stock are entitled to receive dividends, out of the unreserved and unrestricted surplus or net profits of the Company, as declared by the board of directors. No such dividends have been declared as of December 31, 1999 (Note 10) for discussion of the conversion of the outstanding preferred stock subsequent to year-end.

The Company is accreting the issuance costs of the Preferred Stock, which is the difference between the redemption price and the face value of the shares, over the period from the date of sale to the initial

redemption date. Such amount was \$1,920, \$5,737, and \$14,544 for the years ended December 31, 1997, 1998, and 1999, respectively, and is included in interest income in the accompanying statements of operations.

Beneficial Conversion Charge

In accordance with EITF 98-5, the Company recorded a charge in the quarter ending December 31, 1999 of approximately \$79.1 million to reflect the beneficial conversion feature related to the shares of its Series C preferred stock.

6. Related-Party Transactions

A portion of the proceeds from the Predecessor Company's sale of member shares was received from officers, directors, or other parties related to the Predecessor Company. A portion of the cost of the Predecessor Company's purchase of member shares was paid to officers, directors, or other parties related to the Predecessor Company.

A portion of the proceeds from the Company's sales of the Preferred Stock was received from officers, directors, or other parties related to the Company. The sales were conducted concurrently with, and on the same terms as, those entered into with unrelated parties.

7. Commitments And Contingencies

Leases

The Company is obligated under several operating and capital lease agreements, primarily for office space and equipment. Future annual minimum rental payments under these leases as of December 31, 1999 are as follows:

	<u>Operating</u>	<u>Capital</u>
2000	\$ 2,299,014	\$ 261,784
2001	2,300,184	181,345
2002	2,143,020	109,003
2003	1,684,661	25,545
2004	1,290,964	0
Thereafter	2,038,189	0
	<u>\$ 11,756,032</u>	<u>577,677</u>
Less amount representing interest and taxes		<u>76,740</u>
Present value of future minimum capital lease payments		500,937
Less current portion		<u>217,468</u>
Long-term portion		<u>\$ 283,469</u>

Rental expense was \$54,904, \$159,236, and \$629,030 for the years ended December 31, 1997, 1998, 1999, respectively.

Commission Obligation

The Company has entered into license agreements with property owners and/or operators of several office buildings whereby the Company has the right to provide communications services in these buildings. Under the terms of the agreements, the Company is generally obligated to pay a commission based on the

greater of a base fee or a percentage of revenue earned in the related building or development. At December 31, 1999, the Company's aggregate minimum obligation under these agreements is approximately \$130,000 per year for the next seven years.

Purchase Obligation

At December 31, 1999, the Company has contracts with several communications providers with purchase commitments totaling approximately \$1.6 million of which approximately \$1.1 million and \$500,000 are payable in 2000 and 2001, respectively.

Line of Credit

The Company entered into an agreement with Silicon Valley Bank ("Silicon") on September 1, 1998 for a credit line totaling \$500,000 bearing interest at Silicon's prime rate plus 1.25%. The total amount was borrowed and subsequently repaid prior to December 31, 1998. The agreement expired on April 22, 1999. Borrowings were secured by a security interest in certain of the Company's assets.

Employee Benefit Plan

In 1997, the Company adopted a 401(k) defined contribution plan. Participants may elect to defer 15% of compensation up to a maximum amount determined annually pursuant to Internal Revenue Service regulations. The Company may provide matching contributions under this plan, but has not done so in the periods presented.

Legal Proceedings

The Company is subject to legal proceedings and claims that arise in the ordinary course of business. There are no pending legal proceedings to which the Company is a party that management believes will have a material adverse effect on the financial position, results of operations, or cash flows of the Company (Note 10).

8. Income Taxes

On July 15, 1997, the Company recorded a deferred tax liability in the amount of \$73,487 which represents the Predecessor Company's tax consequences of temporary differences in reporting items for financial statement and income tax purposes at the time of the Reorganization (Note 1).

The income tax effects of temporary differences between the carrying amounts of assets and liabilities in the financial statements and their respective income tax bases, which give rise to deferred tax assets and liabilities, as of December 31 are as follows:

	<u>1998</u>	<u>1999</u>
Deferred income tax assets:		
Net operating loss carryforwards	\$ 1,737,863	\$ 7,198,975
Allowance for doubtful accounts	30,218	90,268
Other	14,358	29,119
Total deferred income tax assets	<u>1,782,439</u>	<u>7,318,362</u>
Deferred income tax liabilities:		
Depreciation	(191,419)	(940,989)
Valuation allowance	(1,591,020)	(6,377,373)
Net deferred income taxes	<u>\$ 0</u>	<u>\$ 0</u>

The Company has provided a valuation allowance against its net deferred tax assets, as management has concluded that it is not likely that such assets will be realized in their entirety. The Company had approximately \$19 million of federal and state net operating loss carryforwards at December 31, 1999. The net operating loss carryforwards begin to expire in the year 2017 if not previously utilized. Utilization of existing net operating loss carryforwards may be limited in future years if significant ownership changes occur.

The components of the provision for income taxes for the years ended December 31, 1997, 1998, and 1999 are as follows:

	1997	1998	1999
Current	\$ 0	\$ 0	\$ 0
Deferred	(310,766)	(1,280,254)	(4,786,353)
Increase in valuation allowance	310,766	1,280,254	4,786,353
Total income tax benefit	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 0</u>

The differences between the federal statutory income tax rate and the Company's effective rate for the years ended December 31, 1997, 1998, and 1999 are as follows:

	1997	1998	1999
Federal statutory rate	(34)%	(34)%	(34)%
State income taxes, net of federal benefit	(4)	(4)	(4)
Permanent differences	0	0	4
Increase in valuation allowance	38	38	34
Effective rate	<u>0%</u>	<u>0%</u>	<u>0%</u>

9. Acquisition

On December 8, 1998, the Company acquired substantially all of the assets of MTS Communications (the "MTS Acquisition"), a provider of communications services in California, for total consideration of \$2,574,848 consisting of \$1,904,398 in cash and the assumption of certain capital lease obligations with a fair value of \$670,450. The MTS Acquisition was accounted for as a purchase and the results of operations of MTS Communications have been included since the date of acquisition in the accompanying statements of operations. The purchase price was allocated as follows:

Property and equipment	\$2,060,000
Tenant contracts	430,000
Cost in excess of net assets acquired	84,848
	<u>\$2,574,848</u>

Prior to the MTS Acquisition, the Company advanced \$200,000 to MTS Communications in the form of a secured 8% promissory note to fund working capital requirements of MTS Communications. The note was due March 8, 1999 and was repaid in full.

The following unaudited pro forma results of operations for the years ended December 31, 1997 and 1998 assumes that the MTS Acquisition occurred on January 1, 1997. The pro forma information is presented for informational purposes only and may not be indicative of the actual results had the acquisition occurred on the assumed date, nor is the information necessarily indicative of future results of operations.

	1997	1998
Revenues	\$2,325,428	\$4,485,236
Net loss	(2,006,128)	(3,874,625)
Net loss per common share	\$(0.76)	\$(1.47)

Investment in SiteConnect, Inc.

In November 1999, the Company signed a letter of intent (the "Agreement") to acquire 254,125 shares of common stock, representing less than 20% common stock ownership, of SiteConnect, Inc. ("SiteConnect"), a Seattle-based provider of communications services, for consideration of 281,250 shares of the Company's common stock. The Agreement contains an option for the Company to purchase the remaining outstanding common stock of SiteConnect for approximately \$5 million. The option is exercisable at any time prior to the first anniversary of the closing date of the initial investment. The option is payable in approximately 294,118 shares of the Company's common stock.

10. Events Subsequent To Year-End

Stock Split

In February 2000, a committee appointed by the Company's board of directors approved a 4.5-for-1 stock split with respect to its outstanding common stock. All shares of common stock and per share amounts in the accompanying financial statements have been retroactively adjusted to reflect this split.

Initial Public Offering

On February 15, 2000, the Company completed the sale to the public of 11,500,000 shares of its common stock at a per share price of \$17 for net proceeds of approximately \$179 million (the "IPO"). The Company may have a contingent liability arising from a possible violation of Section 5 of the Securities Act of 1933 in connection with the existence of a hyperlink on its Web site to an audio announcement regarding the IPO. The Company does not believe that the existence of this hyperlink caused a violation of the Securities Act, and if any such claim is asserted, the Company intends to contest the matter vigorously. Accordingly, the Company does not believe that its exposure, if any, resulting from the existence of this hyperlink would be material to its results of operations or financial condition.

Conversion of Preferred Stock

Simultaneous with the closing of the Company's initial public offering and pursuant to the contractual agreements with the preferred stockholders, all shares of the Company's Preferred Stock converted into 32,815,359 shares of common stock. Pro forma stockholders' equity at December 31, 1999, after giving effect to this conversion, would be \$83.6 million (unaudited). Had the conversion of the Preferred Stock occurred at the dates of its sales, net loss per share would have been \$(4.64) (unaudited) for the year ended December 31, 1999.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS AS TO SCHEDULES

We have audited, in accordance with auditing standards generally accepted in the United States, the financial statements of CYPRESS COMMUNICATIONS, INC. included in this Form 10-K and have issued our report thereon dated February 21, 2000. Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The schedule listed in the index is the responsibility of the Company's management and is presented for purposes of complying with the Securities and Exchange Commission's rules and are not part of the basic financial statements. This schedule has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, fairly state in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

ARTHUR ANDERSEN LLP

Atlanta, Georgia

February 21, 2000

CYPRESS COMMUNICATIONS, INC.

SCHEDULES

Allowance for Doubtful Accounts:

	<u>Beg. Balance</u>	<u>Charged to Expense</u>	<u>(Writeoffs)/ Recoveries</u>	<u>Ending Balance</u>
For the Year Ended December 31, 1997.....	\$ 0	\$ 9,945	\$ 0	\$ 9,945
For the Year Ended December 31, 1998.....	\$ 9,945	\$ 69,575	\$ 0	\$ 79,520
For the Year Ended December 31, 1999.....	\$ 79,520	\$ 395,618	\$ (107,333)	\$ 367,805

Deferred Tax Asset Valuation Allowance:

	<u>Beg. Balance</u>	<u>Charged to Expense</u>	<u>Reversals</u>	<u>Ending Balance</u>
For the 5 1/2 ended December 31 1997.....	\$ 0	\$ 310,766	\$ 0	\$ 310,766
For the Year Ended December 31, 1998.....	\$ 310,766	\$ 1,280,254	\$ 0	\$ 1,591,020
For the Year Ended December 31, 1999.....	\$ 1,591,202	\$ 4,786,171	\$ 0	\$ 6,377,373

EXHIBIT 23.1

CONSENT OF INDEPENDENT PUBLIC ACCOUNTANTS

As independent public accountants, we hereby consent to the incorporation by reference of our reports included in this Form 10-K, into the Company's previously filed Registration Statements on Form S-8, No. 333-30004 and No. 333-30504.

ARTHUR ANDERSEN LLP

Atlanta, Georgia
March 29, 2000

CYPRESS COMMUNICATIONS INC

Filing Type: 10-Q
Description: Quarterly Report
Filing Date: May 15, 2000
Period End: Mar 31, 2000

Primary Exchange: NASDAQ - National Market
System
Ticker: CYCO

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2000

Commission file number 0-29281

CYPRESS COMMUNICATIONS, INC.
(Exact name of registrant as specified in its charter)Delaware
(State or other jurisdiction
of incorporation or organization)58-2330370
(I.R.S. Employer
Identification No.)Fifteen Piedmont Center, Suite 710
Atlanta, GA 30305
(Address of principal executive offices, including zip code)(404) 869-2500
(Registrant's telephone number, including area code)

(Former name, if changed since last report)

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

APPLICABLE ONLY TO CORPORATE ISSUERS

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

The number of shares of common stock outstanding at April 28, 2000 was 47,317,014.

Cypress Communications, Inc.

QUARTERLY REPORT ON FORM 10-Q
For the Three Months Ended March 31, 2000

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

CYPRESS COMMUNICATIONS, INC.

BALANCE SHEETS

	DECEMBER 31, 1999	MARCH 31, 2000
	-----	-----
ASSETS		(UNAUDITED)
CURRENT ASSETS:		
Cash and cash equivalents	\$ 69,475,283	\$ 224,344,800
Accounts receivable, net of allowance for doubtful accounts of \$367,808, and \$309,068 in 1999 and		

2000, respectively	1,668,003	1,732,951
Prepaid expenses and other	320,516	727,076
Total current assets	71,461,007	226,800,826
PROPERTY AND EQUIPMENT, net of accumulated depreciation of \$2,731,443 and \$3,683,551 in 1999 and 2000, respectively	27,023,000	35,923,603
OTHER ASSETS:		
Cost in excess of net assets acquired, net of accumulated amortization of \$15,556 and \$17,677 in 1999 and 2000, respectively	75,686	71,525
Tenant contracts, net of accumulated amortization of \$260,775 and \$293,611 in 1999 and 2000, respectively	274,722	138,389
Real estate access rights, net of accumulated amortization of \$0 and \$2,382,211 in 1999 and 2000, respectively	23,398,094	181,412,753
Other	617,020	644,636
Total other assets	24,365,492	185,369,313
Total assets	\$122,854,601	\$ 448,109,242
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$ 12,672,121	\$ 2,643,098
Accrued expenses	2,696,133	4,810,222
Current portion of capital lease obligations	217,468	213,131
Total current liabilities	15,585,722	7,666,451
LONG-TERM PORTION OF CAPITAL LEASE OBLIGATIONS	283,469	230,958
Total liabilities	15,869,191	7,897,409
CONVERTIBLE REDEEMABLE PREFERRED STOCK:		
\$.001 par value; Series A: 1,211,140 and 0 shares issued and outstanding in 1999 and 2000, respectively	6,040,856	0
\$.001 par value; Series B: 1,339,575 and 0 shares issued and outstanding in 1999 and 2000, respectively	10,705,616	0
\$.001 par value; Series B-1: 579,613 and 0 shares issued and outstanding in 1999 and 2000, respectively	4,632,137	0
\$.001 par value; Series C: 4,161,974 and 0 shares issued and outstanding in 1999 and 2000, respectively	78,899,121	0
Total preferred stock	100,277,750	0
STOCKHOLDERS' EQUITY:		
Common stock, \$.001 par value; 58,620,758 and 150,000,000 shares authorized in 1999 and 2000, respectively; 2,759,806 and 47,313,839 shares issued and outstanding in 1999 and 2000, respectively	2,760	47,315
Additional paid-in capital	109,339,640	388,541,336
Warrants outstanding	23,398,094	186,794,965
Deferred compensation	(27,124,350)	(24,833,218)
Accumulated deficit	(98,908,584)	(110,338,565)
Total stockholders' equity	6,707,660	440,211,833
Total liabilities and stockholders' equity	\$122,854,601	\$ 448,109,242
	=====	=====

The accompanying notes are an integral part of these balance sheets.

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CYPRESS COMMUNICATIONS, INC.

STATEMENTS OF OPERATIONS

(UNAUDITED)

FOR THE THREE MONTHS ENDED MARCH 31, 1999 AND 2000

	1999	2000
	-----	-----
REVENUES	\$ 1,581,197	\$ 2,530,680
	-----	-----

OPERATING EXPENSES:		
Cost of services	961,176	2,354,231
Sales and marketing, including noncash compensation expense of \$18,473 and \$272,888 in 1999 and 2000, respectively	616,910	2,425,481
General and administrative, including noncash compensation expense of \$110,305 and \$1,089,587 in 1999 and 2000, respectively	1,403,760	7,924,543
Amortization of real estate access rights	0	2,382,211
Depreciation and other amortization	385,806	1,031,512
Total operating expenses	3,366,652	16,017,978
OPERATING LOSS	(1,785,455)	(13,487,298)
INTEREST INCOME, net	96,353	2,057,318
LOSS BEFORE INCOME TAXES	(1,687,102)	(11,429,980)
INCOME TAX BENEFIT	0	0
NET LOSS	(1,687,102)	(11,429,980)
NET LOSS PER COMMON SHARE:		
Basic and diluted	\$(0.64)	\$(0.41)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING:		
Basic and diluted	2,636,906	27,746,241

The accompanying notes are an integral part of these statements.

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CYPRESS COMMUNICATIONS, INC.

STATEMENTS OF CASH FLOWS

(UNAUDITED)

FOR THE THREE MONTHS ENDED MARCH 31, 1999 AND 2000

	1999	2000
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$(1,687,102)	\$(11,429,980)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and other amortization	385,806	3,413,723
Amortization of deferred compensation	128,778	1,362,475
Changes in operating assets and liabilities:		
Accounts receivable, net	(144,937)	(63,748)
Prepaid expenses and other current assets	(72,852)	(406,759)
Other assets	(23,664)	(127,608)
Accounts payable and accrued expenses	154,940	1,265,496
Net cash used in operating activities	(1,259,031)	(5,986,411)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(1,406,797)	(19,629,701)
Repayment of advance to MTS Communications	200,000	0
Other	19,400	(252,292)
Net cash used in investing activities	(1,187,397)	(19,881,992)
CASH FLOWS FROM FINANCING ACTIVITIES:		

Proceeds from exercise of stock options	0	190,434
Principal payments on capital lease obligations	(48,734)	(56,848)
Proceeds from initial public offering, net of offering costs	0	180,604,129
Net cash (used in) provided by financing activities	(48,734)	180,737,715
(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(2,498,160)	154,869,312
CASH AND CASH EQUIVALENTS, beginning of year	11,057,696	69,475,288
CASH AND CASH EQUIVALENTS, end of year	\$ 8,559,536	\$224,344,600
	=====	=====

The accompanying notes are an integral part of these statements.

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CYPRESS COMMUNICATIONS, INC.

NOTES TO INTERIM FINANCIAL STATEMENTS

(UNAUDITED)

MARCH 31, 1999 AND 2000

1. Organization and Nature of Business

Cypress Communications, Inc. ("Cypress" or the "Company") provides a full range of communications services to small and medium-sized businesses in multi-tenant office buildings. These buildings are located in major metropolitan markets throughout the United States. These communications services include high speed, dedicated Internet access and data services, local and long distance voice services, feature rich digital telephone systems, digital satellite business television, voicemail, e-mail, website hosting, security/monitoring services and other advanced communications services. The Company delivers these services over state-of-the-art fiber-optic, digital and broadband networks that Cypress designs, constructs, owns and operates inside large and medium-sized office buildings.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) necessary to present fairly the information set forth therein have been included. The accompanying condensed consolidated financial statements should be read in conjunction with the financial statements and footnotes included in the Annual Report on Form 10-K of Cypress for the year ended December 31, 1999. Operating results for the three-month period ended March 31, 2000 are not necessarily an indication of the results that may be expected for the year ended December 31, 2000.

3. Capital Transactions

Stock Split

In February 2000, a committee appointed by the Company's board of directors

approved a 4.5-for-1 stock split with respect to its outstanding common stock. All shares of common stock and per share amounts in the accompanying financial statements have been retroactively adjusted to reflect this split.

Initial Public Offering

On February 15, 2000, the Company completed its initial public offering. The Company sold an aggregate of 11,500,000 shares of common stock (including 1,500,000 shares which were issued upon the exercise of the underwriters' overallotment option) at a per share price of \$17.00, for an aggregate offering price of approximately \$195.5 million.

In connection with the initial public offering, the Company incurred offering expenses of approximately \$15.8 million (including underwriting discounts). Approximately \$0.3 million of these expenses were incurred in the fourth quarter of 1999 and the remaining \$15.5 million of expenses were incurred in the first quarter of 2000. After deducting these expenses, the Company received approximately \$179.7 million in net proceeds from the initial public offering. The Company intends to use the proceeds from the offering for working capital and general corporate

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purposes, the construction of in-building networks and the purchase of communications equipment.

Conversion of Preferred Stock

Simultaneous with the closing of the Company's initial public offering, all outstanding shares of the Company's preferred stock automatically converted into 32,815,359 shares of common stock.

4. Real Estate Access Rights

In November and December 1999, the Company entered into master license agreements and stock warrant agreements with several property owners and operators. Under the terms of these agreements, the Company issued warrants to purchase up to an aggregate of approximately 11 million shares of the Company's common stock at a price of \$4.22 per share. These warrants are exercisable for periods of five to ten years. The number of warrants was based on the gross leaseable area of the buildings subject to the master license agreements. The final number of warrants was determined upon the completion of a due diligence period and finalization of the building schedules in the master license agreements. Upon the completion of the due diligence period and the finalization of the building schedules, the Company recorded the fair value of the warrants as an intangible asset, real estate access rights, which is being amortized on a straight-line basis over the terms of the related license agreements, which are generally ten years. Amortization of real estate access rights was \$2,382,211 for the three months ended March 31, 2000.

As of December 31, 1999, the Company had recorded approximately \$23.4 million for the fair value of warrants earned through December 31, 1999. During the three months ended March 31, 2000, the Company recorded an additional \$163.4 million for the fair value of warrants earned during that period.

5. Subsequent Events

Real Estate Access Rights

In April 2000, the Company entered into an additional master license agreement and a stock warrant agreement with a property owner and operator. Under the terms of these agreements, the Company issued warrants to purchase up to an aggregate of 74,000 shares of the Company's common stock at an exercise price of \$04.67 per share. These warrants are exercisable for a period of 10

years. The exact number of shares of common stock underlying the warrants, which is based on the gross leaseable area of the buildings set forth in the master license agreement, will be determined upon the completion of a due diligence period and the finalization of the building schedules, which is expected to be complete in June 2000. The measurement date for valuing the warrants will be the date(s) upon which the property owner and operator enters into communications license agreements with the Company. The fair market value of warrants earned will be recorded as an intangible asset, real estate access rights, and will be amortized over the terms of the related communications license agreements, which are expected to be ten years.

SiteConnect Acquisition

In April 2000, the Company acquired all of the outstanding common stock of SiteConnect, Inc., a Seattle-based in-building communications service provider, in exchange for approximately 581,450 shares of the Company's common stock. The number of shares of the Company's common stock issued in connection with the acquisition may be increased or decreased based on certain post-closing adjustments.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Overview

We provide a full range of broadband communications services to small and medium-sized businesses located in multi-tenant office buildings in major metropolitan markets in the United States. This comprehensive bundle of services currently includes high-speed dedicated Internet access, local and long distance voice services, digital telephone systems, business television, voicemail, e-mail, web hosting and other advanced services. Since the inception of our predecessor company in August 1995, our principal activities have included securing license agreements with building owners and real estate managers that enable us to install our in-building fiber-optic, digital and broadband networks, marketing our communications services to tenants and hiring qualified personnel to support our rapid growth. We began operating in-building networks in June 1996 and as of March 31, 2000, we were providing services in approximately 200 buildings representing approximately 55 million rentable square feet. To date, we have secured agreements giving us the right to operate our networks in over 800 buildings representing more than 230 million rentable square feet.

Results of Operations

Three Months Ended March 31, 2000 Compared to the Three Months Ended March 31, 1999

Revenues. Revenues for the three months ended March 31, 2000 increased 60% to \$2.5 million from \$1.6 million for the same period in the prior year. The increase in revenues relates to the addition of new customers and providing additional services to existing customers.

Cost of Services. Cost of services for the three months ended March 31, 2000 increased 145% to \$2.4 million from \$1.0 million for the same period in the prior year. The increase in cost of services was due primarily to an increase in the number of leased facilities connecting our licensed buildings to local, long distance and Internet providers and the greater volume of voice and data traffic. As of March 31, 2000, we had networks installed in approximately 200 buildings versus approximately 50 buildings installed at March 31, 1999.

Sales and Marketing Expenses. Sales and marketing expenses for the three months ended March 31, 2000 increased 293% to \$2.4 million from \$0.6 million for the same period in the prior year. \$1.1 million of this increase in expenses was due to an increase in the number of sales and marketing personnel and their

related compensation and expenses; \$0.1 million of this increase was due to increased revenue sharing payments made to property owners with whom we have license agreements; \$0.3 million of this increase was due to increased promotion of our services via direct marketing and advertising in our licensed buildings and \$0.3 million of this increase was due to an increase in amortization of non-cash deferred compensation expense related to the issuance of stock options at exercise prices lower than fair value on their dates of grant. We expect sales and marketing expenses to continue to grow as we hire additional personnel and incur additional expenses to market our services to potential customers.

General and Administrative Expenses. General and administrative expenses for the three months ended March 31, 2000 increased 457% to \$7.8 million from \$1.4 million for the same period in the prior year. The increase in general and administrative expenses was due to a \$3.9 million increase in salaries, benefits and recruiting and training expenses related to the hiring of additional personnel, a \$1.0 million increase in amortization of non-cash deferred compensation related to the issuance of stock options at exercise prices lower than fair value on their dates of grant, a \$0.3 million increase in travel and entertainment expenses primarily related to marketing to property owners and operators and expenses associated with personnel traveling to oversee and conduct the installation of our networks in additional buildings, a \$0.2 million increase in accounting, consulting, legal and billing outsourcing fees, and a \$1.0 million increase in office space rent and other growth-driven operating expenses. We expect general and administrative expenses to continue to grow as we hire additional personnel and incur additional expenses to support the growth of our operations.

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Amortization of Real Estate Access Rights. The amortization of real estate access rights represents the amortization of the value of warrants issued to property owners or operators over the terms of the related license agreements, which are generally ten years. Amortization of these amounts began in the first quarter of 2000. See note 4 to our interim financial statements.

Depreciation and Other Amortization. Depreciation and other amortization for the three months ended March 31, 2000 increased 167% to \$1.0 million from \$0.4 million for the same period in the prior year. \$0.5 million of this increase was due to increased capital expenditures related to deploying our in-building networks and related equipment, and \$0.1 million of this increase was due to depreciation of computers and other back-office equipment.

Interest Income, net. Interest income, net for the three months ended March 31, 2000 increased to \$2.0 million from \$0.1 million for the same period in the prior year. The increase in interest income, net was due to interest income on short-term interest bearing investments as a result of investing the proceeds of our Series C preferred stock offering in the third quarter of 1999 and initial public stock offering of common stock in February 2000. Interest expense was nominal in both periods.

Liquidity and Capital Resources

The results of our operations have generated a net cash outflow due to the rate at which we have grown. Cash flow from operations totaled \$(1.3 million) and \$(6.0 million) for the three months ended, March 31, 1999, and 2000, respectively. The expansion of our operating and administrative personnel, office space costs, and other operating expenses were the principal contributors to the increases in the net cash outflow between the periods. As we continue to expand our operations, these increases in period-over-period operating cash outflows are expected to continue.

Cash used in investing activities was \$(1.2 million) and \$(19.9 million) for the three months ended March 31, 1999 and 2000, respectively. Cash used in investing activities has primarily been expended to construct our in-building networks. As of March 31, 2000, we had made capital expenditures of

approximately \$34.6 million since inception. We expect that capital expenditures will increase substantially in future periods as we construct our networks and purchase more communications equipment. We will continue to seek access to additional buildings. If we are successful in gaining access to additional buildings, we will have substantial needs for additional capital for an indefinite period. We also expect to have substantial and increasing negative adjusted EBITDA and net losses.

Cash provided by financing activities was \$(0.01 million) and \$180.7 million and for the three months ended March 31, 1999 and 2000, respectively. Cash provided by financing activities during the three months ending March 31, 2000 was from the Company's initial public offering in which we sold 11,500,000 shares of our common stock at \$17 per share, netting proceeds of approximately \$180.6 million after deducting first quarter offering expenses (approximately \$0.3 million of offering expenses were incurred in the fourth quarter of 1999). We intend to use the net proceeds from this offering for construction of in-building networks and the purchase of communications equipment and for implementation and modification of information support systems. The remainder of the net proceeds will be available for working capital and general corporate purposes. We may also use a portion of the net proceeds to acquire or invest in complementary businesses, technologies, services or products. However, we currently have no material commitments or agreements with respect to any of these types of transactions.

During the first quarter of 2000, we recorded an additional \$163.4 million for warrants that were earned during the three months ended March 31, 2000, which are exercisable for an aggregate of approximately 9.5 million shares of our common stock at an exercise price of \$4.22 per share. These warrants were issued to several property owners and operators in connection with their execution of master license agreements in November and December 1999. See note 4 to our interim financial statements. These master license agreements gave us the right to operate our networks in more than 600 buildings representing more than 194 million rentable square feet.

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In April 2000, the Company acquired all of the outstanding common stock of SiteConnect, Inc., a Seattle-based in-building communications service provider, in exchange for approximately 581,450 shares of the Company's common stock. The number of shares of the Company's common stock issued in connection with the acquisition may be increased or decreased based on certain post-closing adjustments.

We are currently operational in 17 markets, and plan to expand our presence to approximately 27 markets by the end of 2000 and approximately 50 markets by the end of 2001. We estimate that this expansion will require capital expenditures of approximately \$50.0 million in 2000 and approximately \$90.0 million in 2001.

We estimate that the net proceeds from our initial public offering in addition to cash on hand will be sufficient to fund operations and the projected deployment of our network through mid-2001. We do, however, expect to continue our growth, expansion and the further development of our network and services beyond that point. Accordingly, we expect that we will eventually need to arrange for additional sources of capital through the issuance of debt or equity or bank borrowings. There are no commitments for any such additional financing, and we cannot be sure that we will be able to obtain any such additional financing at the times required and on acceptable terms and conditions. In such event, our growth could slow and operations could be adversely affected.

The actual amount and timing of our future capital requirements may differ materially from our estimates as a result of many factors, some of which we cannot control. These factors include:

- . the timing of execution of license agreements;
- . the ability to meet or exceed construction schedules;

- . the ability to obtain favorable prices for purchases of equipment;
- . our ability to develop, acquire and integrate the necessary operational support systems;
- . the cost of network development in each of our markets;
- . demand for our services;
- . the successful deployment of new services that we may offer;
- . the timing and extent of future acquisitions or investments, if any, and our ability to integrate these acquisitions or investments;
- . regulatory changes; and
- . changes in technology and competitive developments beyond our control.

Recent Accounting Pronouncements

The Securities and Exchange Commission has released SAB No. 101, "Revenue Recognition in Financial Statements." We are reviewing our policies with respect to SAB No. 101 and do not anticipate the impact of adoption to be material.

Risks Associated with Forward-Looking Statements Included in this Form 10-Q

This Report on Form 10-Q contains forward-looking statements, including, without limitation, statements about our plans, objectives, expectations, intentions, assumptions and prospects. You can identify forward-looking statements by the use of words such as "expect," "anticipate," "intend," "plan," "believe," "seek," "estimate," "assume" and similar expressions which predict or indicate future events and trends which do not relate to historical matters.

You should not rely on forward-looking statements because they involve known and unknown risks, uncertainties and other factors, some of which are beyond our control. These risks, uncertainties and other factors may cause our actual results, performance or achievements to differ materially from the anticipated future results, performance or achievements expressed or implied by the forward-looking statements. These risks, uncertainties and factors, include, without limitation, our ability to obtain additional license agreements with property owners and managers, the intense competition for our service offerings, our dependence on growth in demand for our services, our ability to manage the growth of our operations and our ability to raise additional capital. In addition, the factors described under "Risk Factors That May Affect Future Results" in our Annual Report on Form

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10-K for the year ended December 31, 1999 may result in these differences. You should carefully review all of these factors, and you should be aware that there may be other factors that could cause these differences. These forward-looking statements represent our estimates and assumptions only as of the date of this report, and we do not undertake to update these forward-looking statements to reflect future events or developments.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Our exposure to financial market risk, including changes in interest rates, relates primarily to our investment portfolio. We typically do not attempt to reduce or hedge the market exposure on our investment securities because our investments are in fixed-rate, short-term securities. We do not have any derivative instruments. The fair value of our investment portfolio or related income would not be significantly impacted by either a 100 basis point increase or decrease in interest rates due mainly to the fixed-rate, short-term nature of our investments. As of March 31, 2000, we had no debt outstanding, other than capital leases.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

We are not currently involved in any pending legal proceedings that are expected to have a material adverse effect on our business.

Item 2. Changes in Securities and Use of Proceeds.

We completed our initial public offering in February 2000. The initial public offering was made pursuant to a Registration Statement on Form S-1, originally filed with the Securities and Exchange Commission on December 3, 1999, as amended (Commission File No. 333-92011), which was declared effective on February 9, 2000. The initial public offering commenced on February 10, 2000 and terminated shortly thereafter, after the sale into the public market of all of the registered shares of common stock.

The shares of common stock sold in the initial public offering (including 1,500,000 shares which were issued upon the exercise of the underwriters' overallotment option) were offered for sale by a syndicate of underwriters represented by Bear, Stearns & Co. Inc., Donaldson, Lufkin & Jenrette Securities Corporation and J.C. Bradford & Co.

We registered an aggregate of 11,500,000 shares of common stock (including 1,500,000 shares which were issued upon the exercise of the underwriters' overallotment option) for sale in the initial public offering at a per share price of \$17.00, for an aggregate offering price of approximately \$195.5 million.

We incurred the following expenses in connection with the initial public offering:

Underwriting discounts and commissions of approximately:	\$13,685,000
Other expenses of approximately:	\$ 2,108,000

Total expenses of approximately:	\$15,793,000
	=====

No payments were made to (i) any of our directors, officers, general partners or associates, (ii) any person(s) owning 10% or more of our common stock, or (iii) any of our affiliates.

After deducting the expenses set forth above, we received approximately \$179.7 million in net proceeds from the initial public offering. We have not yet used any of the net proceeds from the initial public offering. The net proceeds have been invested in cash, cash equivalents and short-term investments. Consistent with the description of the use of proceeds set forth in the prospectus contained in the Registration Statement, we intend to use the proceeds from the offering for working capital and general corporate purposes, the construction of in-building networks and the purchase of communications equipment.

Item 3. Defaults Upon Senior Securities.

None.

Item 4. Submission of Matters to a Vote of Security Holders.

On February 8, 2000, our stockholders, in connection with our initial public offering, approved the filing of the Second Amended and Restated

Certificate of Incorporation by written consent in lieu of a special meeting.
On the date of such

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consent there were 35,791,124 shares of common stock outstanding, and stockholders holding 35,791,124 shares of common stock executed such consent, representing 100.0% of the then outstanding shares of common stock.

Item 5. Other Information.

None.

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits

27.1 Financial Data Schedule

(b) Reports on Form 8-K

There were no reports filed by the Company on Form 8-K during the quarter ended March 31, 2000.

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SIGNATURES

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

CYPRESS COMMUNICATIONS, INC.

Date: May 15, 2000

By: /s/ Barry L. Boniface

Barry L. Boniface
Vice President, Chief Financial
Officer and Treasurer

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FINANCIAL STATEMENTS OF
CYPRESS COMMUNICATIONS OPERATING COMPANY, INC.
FOR THE PERIOD ENDED APRIL 30, 2000

HIGHLY CONFIDENTIAL

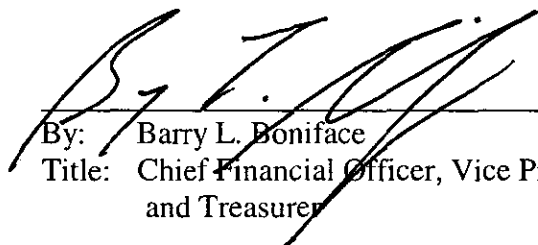
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GUARANTY

I, Barry L. Boniface, am the Chief Financial Officer, Vice President and Treasurer of Cypress Communications, Inc. and am authorized to make this Guaranty on its behalf. Cypress Communications, Inc. is the parent company of Cypress Communications Operating Company, Inc. ("Cypress"), the Applicant herein.

Cypress Communications, Inc. hereby guarantees the financial obligations of Cypress attendant to Cypress' operations as a telecommunications carrier in the State of Missouri. Cypress Communications, Inc. issues this Guaranty in support of Cypress' Application before the Missouri Public Service Commission for a Certificate of Authority to provide all forms of basic local telecommunications services in the State of Missouri.

Cypress Communications, Inc.

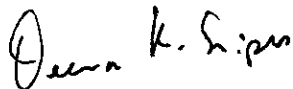

By: Barry L. Boniface
Title: Chief Financial Officer, Vice President
and Treasurer

State of Georgia)
) ss.
County of Fulton)

The above-named Barry L. Boniface appeared before me today and swore that he is the Chief Financial Officer, Vice President and Treasurer of Cypress Communications, Inc. and is duly authorized by it to execute the foregoing Guaranty on its behalf.

Subscribed and Sworn to me this 8th day of June, 2000.

Notary Public



My Commission expires 12-16-01

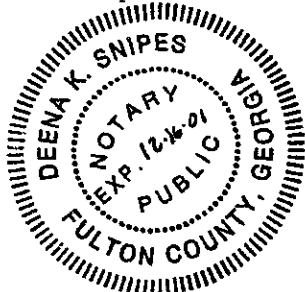


EXHIBIT 3

Managerial Qualifications

Biographies of Key Personnel of Cypress Communications Operating Co., Inc.

W. Frank Blount

Director, Chairman and Chief Executive Officer

W. Frank Blount has served as our Chairman and Chief Executive Officer and a director since June 2000. From January 1992 until March 1999, Mr. Blount served as Chief Executive Officer of Telstra Communications Corporation, Australia's principal telecommunications company and the 11th largest telecommunications company in the world. Prior to joining Telstra, he served in various executive positions for AT&T, including Group President of the Communications Products Group and President of the Network Operations Group. Mr. Blount also has held senior positions in engineering, plant operations, marketing and network operations at Southern Bell Telephone Company. Mr. Blount currently serves as a director of Hanson's UK, Alcatel USA and Alcatel France, Entergy Corporation, Adtran, Inc. and Caterpillar, Inc. Mr. Blount received a Bachelor of Science degree from Georgia State University and a Master of Science degree from the Massachusetts Institute of Technology.

R. Stanley Allen

Director, Vice Chairman

R. Stanley Allen is a co-founder of the Company and has served as our Chief Executive Officer and a director since August 1995. From August 1995 until September 1998, he also served as our President. From March 1994 to May 1996, Mr. Allen was President and Chief Executive Officer of Applied Video Technologies, Inc., a wireless cable and communications investment and development company. From 1991 to 1994, Mr. Allen was President of American Quality Cable Corporation, a wireless cable television operator. Mr. Allen has also held positions as Manager-Real Estate Consulting for Coopers & Lybrand and Analyst for Wellington Real Estate, an affiliate of Boston-based Wellington Management Company. Mr. Allen was a Director for Wireless Cable of Atlanta before its acquisition by BellSouth in 1997 and was also a Director for the Wireless Cable Association. Mr. Allen received a Bachelor of Arts degree in Economics and a Master of Business Administration degree from the University of Virginia.

Mark A. Graves

Director, President, Chief Operating Officer and Secretary

Mark R. Graves has served as our President since September 1998 and our Chief Operating Officer and Secretary since September 1997. From September 1997 until September 1998, he also served as our Chief Financial Officer. From March 1994 to September 1997, Mr. Graves was Executive Director of Corporate Development for BellSouth Corporation, where he was involved in mergers, acquisitions and other strategic transactions. Mr. Graves' activities principally involved BellSouth Corporation's telephone services, Internet services unit and wireless data partnerships. From May 1989 to February 1994, Mr. Graves was a Principal at Sterling Payot

Company, a private investment firm in San Francisco, where he provided advisory services in strategy and finance predominantly to media and telecommunications companies, including Pacific Telesis in its spin-off of PacTel Corp., which was renamed AirTouch Communications. Prior to joining Sterling Payot Company, Mr. Graves held positions at The First Boston Corporation and United Technologies Corporation. Mr. Graves received a Bachelor of Arts degree in Economics and a Master of Business Administration degree from Harvard University.

Barry L. Boniface

Director, Chief Financial Officer, Vice President and Treasurer

Barry L. Boniface has served as our Chief Financial Officer since October 1998. From September 1994 to October 1998, Mr. Boniface was Executive Director of Corporate Development for BellSouth Corporation, where he was responsible for domestic and international mergers, acquisitions, divestitures and other strategic transactions. Mr. Boniface's activities principally involved BellSouth's domestic and international wireless telephone services and competitive local telephone activities. Prior to that, Mr. Boniface was a principal in Berkshire Partners, Inc., a merchant banking firm based in Dallas, Texas. He has also held the positions of Chief Operating Officer for Global Business Acceleration, Inc., an early stage software development company, and Vice President in the Corporate Finance Department at Principal Financial Securities, Inc., an investment banking firm. Mr. Boniface received a Bachelor of Business Administration degree in Management Information Systems from Southern Methodist University and a Master of Business Administration degree from the Goizueta School at Emory University.

Ward C. Bourdeaux

Director, Executive Vice President

Ward C. Bourdeaux, Jr. is a co-founder of the Company and has served as our Executive Vice President and a director since August 1995. From January 1993 to April 1995, Mr. Bourdeaux served as Director of Development for RealCom Office Communications, where he was responsible for identifying new building and market opportunities and entering into new license agreements on a national basis, and for the renewal of existing agreements nationally. Prior to that, he spent over nine years in the commercial real estate industry with Cushman & Wakefield and Carter & Associates. Mr. Bourdeaux received a Bachelor of Arts degree in Communications from the University of Alabama.

C. Timothy Allaway

Vice President of Customer Service

C. Timothy Allaway has served as our Vice President of Customer Service since December 1999. From June 1996 to December 1999, Mr. Allaway as Director, Customer Services for IBM, North America supporting the full line of hardware and software offerings. From September 1994 to June 1996, Mr. Allaway was Director, Small

Business Sales and Partnerships for MCI. From 1986 to September 1994, Mr. Allaway held various sales and services management positions for MCI. Prior to that, Mr. Allaway spent five years with Xerox Corporation. Mr. Allaway received a Bachelor of Science degree in Management from Jacksonville State University and a Master of Business Administration degree from Auburn University.

Eugene H. Kreeft

Vice President of Engineering

Eugene H. Kreeft has served as our Vice President of Engineering since February 1999. From 1991 until February 1999, Mr. Kreeft was an Executive Vice President of Preferred Networks, Inc., an outsourcing services provider to the wireless industry which he founded in 1991. From 1989 to 1991, Mr. Kreeft served as Director of Technical Support, U.S. Operations, for Glenayre Technologies, a developer and provider of personal telecommunications systems. Prior to that, Mr. Kreeft was employed by BBL Industries, Inc., a paging equipment manufacturer, where he served as both Vice President of Engineering and Manufacturing and Vice President of Applications/New Product Development. Mr. Kreeft has also held management and engineering positions with Motorola, RAM Broadcasting, AT&T, Western Union Microwave Systems, Highland Telephone Company and Delaware Telephone Company.

Robert W. McCarthy

Vice President, General Counsel and Assistant Secretary

Robert W. McCarthy has served as our Vice President, General Counsel and Assistant Secretary since December 1999. From August 1996 until December 1999, Mr. McCarthy was a General Attorney at BellSouth Corporation, where he specialized in domestic and international mergers and acquisitions and joint venture transactions. Prior to that, he was a partner in the Atlanta offices of Hunton & Williams, where he specialized in mergers and acquisitions, joint ventures and venture capital transactions. Mr. McCarthy received a Bachelor of Arts degree in Political Science and a Juris Doctor degree from the University of North Carolina at Chapel Hill.

James W. McClintock

Vice President of International

James H. McClintock has served as our Vice President of International since December 1999. From March 1999 until December 1999, Mr. McClintock was Vice President of Data Services for BellSouth International (BSI), where he led the development of BSI's Internet and data strategy and associated business development activities, focusing principally on Latin America and Europe. Prior to that, Mr. McClintock was Executive Director of Corporation Development for BellSouth Corporation, where he worked primarily with BellSouth Entertainment and BellSouth.net, managing a number of significant merger, acquisition and alliance activities involving these two business units. Prior to joining BellSouth in 1993, Mr. McClintock had fourteen years of experience managing, investing in and financing

entrepreneurial ventures of all types and scale, including positions in banking with Citicorp and in venture capital with Equity Group Investments. Mr. McClintock received a Bachelor of Arts degree in Economics from Washington and Lee University and a Master of Business Administration degree in Finance from the University of North Carolina.

Raymond F. Potts

Vice President of Marketing and Sales

Raymond F. Potts has served as our Vice President of Marketing and Sales since October 1999. From September 1997 to October 1999, Mr. Potts was Regional Vice President for Sales, Operations and Marketing for the Midwest territory of Teligent, Inc., a wireless telecommunications company. From 1996 to September 1997, Mr. Potts served as Vice President of Sales for the Midwest region of Cable & Wireless, Inc., a wireless telecommunications company. Prior to that, Mr. Potts spent in excess of ten years in various senior-level sales and service management positions for Midcom Communications, Sprint, LCI and TFN Communications. Mr. Potts received a Bachelor of Business Administration degree from St. Joseph's College in Rensselaer, Indiana.

Claire S. Schenk

Vice President of Human Resources

Claire S. Schenk has served as our Vice President of Human Resources since November 1999 and prior to that served as our Director of Human Resources from June 1999 to November 1999. From June 1996 until May 1999, Ms. Schenk was Vice President from Human Resources for Trism, Inc., a national specialized transportation company headquartered in Atlanta. From December 1989 until June 1996, Ms. Schenk was Vice President, Senior Business Partner for two national mortgage companies. Ms. Schenk also has ten years of human resources management experience with Sheraton Corporation and Six Flags Corporation. Ms. Schenk received a Bachelor of Arts degree in Psychology from Emory University.

Alistair Sloan

Vice President of Internet Services

Alistair Sloan has served as our Vice President of Internet Services since September 1999. From January 1998 until September 1999, Mr. Sloan was our Manager of Internet Services. Prior to joining Cypress, Mr. Sloan was Project Manager at Systems Atlanta, where he consulted with clients on Internet and Wide Area Networking design and security. Prior to that, Mr. Sloan was a manager of Internet Connect, a division of Systems Atlanta specializing in dedicated business Internet connectivity. Mr. Sloan has also held positions with Ingram Micro, Inc. and has been an independent consultant in the field of local area networking. Mr. Sloan received a Bachelor of Arts degree in Political Science from the University of Bridgeport.

AFFIDAVIT

STATE OF GEORGIA

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COUNTY OF FULTON

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I declare under penalty of perjury that I, Barry L. Boniface, am Chief Financial Officer, Vice President and Treasurer of Cypress Communications, Inc., the Applicant; that I am authorized to make this verification on the Applicant's behalf; that I have read the foregoing Application and know the contents thereof; and that the same are true of my knowledge, except as to the matters which are therein stated on information or belief, and as to those matters I believe them to be true.

BY: Barry L. Boniface
TITLE: Chief Financial Officer, Vice President and Treasurer

Subscribed and sworn to before me this 8th day of June, 2000.

Deena K. Snipes

Notary Public

My Commission Expires: 12-16-01

