



DIVIDER

STATE OF NORTH DAKOTA
INFORMATION TECHNOLOGY DEPARTMENT
SFN 2053 (4-2002)

PU-2079-00-655

Z-Tel Communications, Inc.

Local Exchange

Public Convenience & Nece

Filed 12/5/2000

Closed 3/15/2001

00



LAW OFFICES OF

PRINGLE & HERIGSTAD, P.C.

BREMER BANK BUILDING
20 SW 1ST STREET
POST OFFICE BOX 1000
MINOT, NORTH DAKOTA 58702
(701) 852-0381
FAX (701) 857-1361
E-mail: pringle@ndak.net

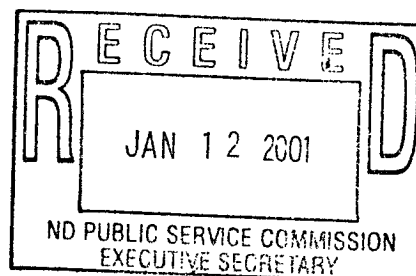
ROGER O. HERIGSTAD
MARK F. PURDY
JAN M. SEBBY
DONALD A. NEGAARD
JAMES E. NOSTDAHL
JOHN J. PETRIK
CAROL K. LARSON
DAVID J. HOGUE
REED A. SODERSTROM
MARK R. HAYS

DONALD T. CAMPBELL
MICHAEL A. BOSH
BRENT M. OLSON
DENISE C. HAYS
DEBRA L. HOFFARTH

OF COUNSEL
HERBERT L. MESCHKE

RETIRED
THOMAS A. WENTZ

January 11, 2000



Jon Mielke, Executive Secretary
Public Service Commission
600 E. Boulevard Ave.
Bismarck, ND 58505-0480

**Z-TEL COMMUNICATIONS, INC. PC&N APPLICATION
CASE NO. PU-2079-00-655**

On behalf of the "Rural Telephone Company Group," we file the enclosed Comments (original plus seven copies) regarding Z-Tel Communications, Inc.'s application for a certificate of public convenience and necessity to provide facilities-based local telecommunications services "throughout North Dakota."

Very truly yours,

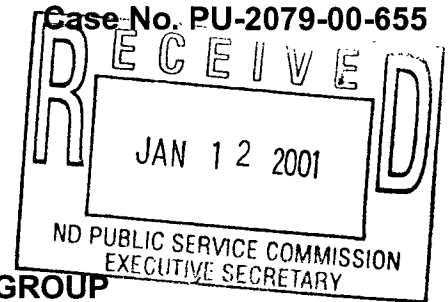
Michael A. Bosh
Pringle & Herigstad, P.C.

jb
encs.

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

Z-Tel Communications, Inc.
Local Exchange
Public Convenience and Necessity

COMMENTS
OF
RURAL TELEPHONE COMPANY GROUP



The Rural Telephone Company Group (RTCG) is a group of telecommunications carriers, each of which is an “incumbent local exchange carrier” and a “rural telephone company” under the federal Telecommunications Act of 1996 (the Act) and each has legal interests in this case under the Act.

The Rural Telephone Company Group includes:

BEK Communications Cooperative and BEK Communications I Inc.
Consolidated Telcom
Dakota Central Telecommunications Cooperative and Dakota Central Telecom I
Dickey Rural Telephone Cooperative and Dickey Rural Communications, Inc.
Inter-Community Telephone Company, LLC and Inter-Community Telephone
Company II, LLC
Midstate Telephone Company and Midstate Communications, Inc.
North Dakota Telephone Company
Northwest Communications Cooperative
Polar Communications Mutual Aid Corporation and Polar Telecommunications, Inc.
Red River Rural Telephone Association and Red River Telecom, Inc.
Reservation Telephone Cooperative
SRT Communications, Inc.
United Telephone Mutual Aid Corporation and Turtle Mountain Communications
West River Telecommunications Cooperative

In PSC Case No. PU-453-96-83, AT&T applied for and was granted a certificate of public convenience and necessity to provide local telecommunications service throughout the State of North Dakota, subject to limitations in the Commission’s Order:

“8. Public convenience and necessity requires the granting of a statewide certificate to AT&T to provide local service. However, the Commission’s determination of the public interest with regard to the service territories of

rural telephone companies is subject to any future proceedings under §251(f)(1) or (2) of the Act.

9. Granting AT&T's application for a statewide certificate is not a ruling that affects the rights of specific rural telephone company pursuant to 47 U.S.C. §251(f)."

In PSC Case No. PU-987-96-390, Sprint applied for and was granted a certificate of public convenience and necessity to provide local telecommunications service throughout the State of North Dakota, subject to limitations based on the precedent established in the AT&T case:

"One issue which has been addressed in other Certificate of Public Convenience and Necessity cases was raised by the intervener, NDATEC. This issue concerns rural telephone companies and what effect the grant of a certificate would have on them. NDATEC identified its interest in this proceeding, and the interests of its members, as a concern that the grant of a certificate of public convenience and necessity not defeat the rural protections provided by the Telecommunications Act of 1996.

The Commission agrees with NDATEC that the question is important and must be addressed. This issue will apply to all certificate requests affecting any service area of any rural telephone company in North Dakota. It is the opinion of the Commission that in all such cases, any determination of public interest is subject to future proceedings regarding rural protections or exemptions.

In the instant case the Commission will adhere to the precedent established in the AT&T certificate case, Docket No. PU-453-96-83, on this issue. In AT&T, the Commission held that its determination of the public interest with regard to the service territories of rural telephone companies is subject to any future proceedings under Section 251(f)(1) or (2) of the Telecommunications Act of 1996 (47 U.S.C. §251(f)(1) or (2)). The Commission also held that granting the certificate on a statewide basis is not a ruling that affects the rights of specific rural telephone companies under 47 U.S.C. §251(f). Both Sprint and NDATEC agree that the qualifications expressed in the AT&T case appropriately apply to Sprint's request for a statewide certificate of public convenience and necessity. The inclusion of these conditions satisfies NDATEC's concerns, and is not objectionable to Sprint."

The AT&T precedent has been cited at least one time following the Sprint case, in Case No. PU-1693-97-269, where a statewide certificate was granted to Eclipse Communications Corp (a subsidiary of Western Wireless Corporation), subject to the rights of rural telephone companies under 47 U.S.C. 251(f).

In reliance on the precedent established by the Commission in the AT&T, Sprint and Eclipse/Western Wireless cases, the RTCG does not request intervention and does not request a hearing on the pending application. The RTCG does request that any order issued to grant the pending application should include limitations substantially the same as those in the AT&T, Sprint and Eclipse/Western Wireless cases, to preserve the "rural safeguard" rights of rural telephone companies under 47 U.S.C. 251(f).

Dated this 11th day of January, 2001.

PRINGLE & HERIGSTAD, P.C.

By Michael A. Bosh

Michael A. Bosh (ND #5313)

Attorneys for RTCG

Bremer Bank Bldg., 2nd Floor

20 - 1st Street SW

P.O. Box 1000

Minot, ND 58702-1000

CERTIFICATE OF SERVICE

A true and correct copy of the foregoing Comments of Rural Telephone Company Group was, on the 11th day of January, 2001, mailed to:

Monique Byrnes
Technologies Management, Inc.
P.O. Drawer 200
Winter Park, FL 32790-0200

Michael A. Bosh
Michael A. Bosh

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

Z-Tel Communications, Inc.
Local Exchange
Public Convenience & Necessity

Case No. PU-2079-00-655

AFFIDAVIT OF SERVICE BY CERTIFIED MAIL

STATE OF NORTH DAKOTA
COUNTY OF BURLEIGH

Sharon Helbling deposes and says that:

she is over the age of 18 years and not a party to this action and, on the **21st day of December, 2000**, she deposited in the United States Mail, Bismarck, North Dakota, **one** envelope with certified postage, return receipt requested, fully prepaid, securely sealed and each containing a photocopy of:

Notice of Opportunity for Hearing

The envelope was addressed as follows:

Monique Byrnes
Technologies Management Inc
P O Drawer 200
Winter Park FL 32790-0200
Cert. No. 7000 0520 0022 8653 3010

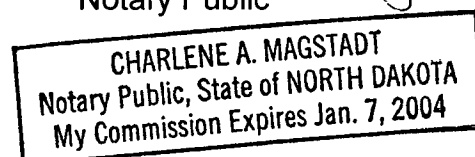
Each address shown is the respective addressee's last reasonably ascertainable post office address.

Subscribed and sworn to before me
this **21st day of December, 2000**.




Notary Public

SEAL



Scott, Sandi L.

From: Bauske, Shelly A.
Sent: Thursday, June 07, 2001 10:03 AM
To: Geiger, Gloria A.; Scott, Sandi L.
Subject: Money Received.....

Case No. PU-2271-01-87
Sprint
\$55.04

Case No. PU-2079-00-655
Z-Tel Communications
\$243.41

- 11** **PU-2271-01-87** Pages: 0
\$55.04 received
by Sprint Communications Co. LP dba Sprint Communi
06/07/2001 CC: Comm Legal Illona Jerry .
- 19** **PU-2079-00-655** Pages: 0
\$243.41 received
by Z-Tel Communications, Inc.
06/07/2001 CC: Comm Legal Illona Jerry .

APPROVED

DATE: 4-25-01
KMF

MOTION

April 25, 2001

Z-Tel Communications, Inc.
Local Exchange
Public Convenience & Necessity

Case No. PU-2079-00-655

I move the Commission bill Z-Tel Communications, Inc. for costs incurred to date in Case No. PU-2079-00-655, Z-Tel Communications, Inc., Local Exchange, Public Convenience & Necessity.



Public Service Commission

State of North Dakota

COMMISSIONERS

Susan E. Wefald, President
Leo M. Reinbold
Anthony T. Clark

Executive Secretary
Jon H. Mielke

600 E Boulevard Ave. Dept. 408
Bismarck, North Dakota 58505-0480
web: www.psc.state.nd.us
e-mail: sab@oracle.psc.state.nd.us
TDD 800-366-6888
Fax 701-328-2410
Phone 701-328-2400

April 25, 2001

Monique Byrnes
Technologies Management Inc
PO Drawer 200
Winter Park FL 32790-0200

RE: Case No. PU-2079-00-655
Z-Tel Communications, Inc.
Local Exchange
Public Convenience & Necessity

Enclosed is a copy of the statement approved at the April 25, 2001 Public Service Commission meeting for the expenses incurred to date in Case No. PU-2079-00-655.

Under N.D.C.C. 49-21-01.7, these expenses are billed through the Valuation Fund and must be paid for by the telecommunications company involved.

Please make your check payable to the Public Service Commission.

Sincerely,

Gloria Geiger
Administrative Assistant
701-328-2401

Enc.

Billing Statement

April 25, 2001

Z-Tel Communications, Inc.
Local Exchange
Public Convenience & Necessity

Case No. PU-2079-00-655

Expenses Incurred to Date:

Advertising Costs	\$243.41
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Amount Due:

Z-Tel Communications, Inc.	\$243.41
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Send Payment and a Copy of this Statement To:

Public Service Commission
600 E Boulevard Ave Dept 408
Bismarck ND 58505-0480

Federal Tax ID 45-0309764

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

Z-Tel Communications, Inc.
Local Exchange
Public Convenience & Necessity

Case No. PU-2079-00-655

AFFIDAVIT OF SERVICE BY CERTIFIED MAIL

STATE OF NORTH DAKOTA
COUNTY OF BURLEIGH

Sharon Helbling deposes and says that:

she is over the age of 18 years and not a party to this action and, on the **15th day of March, 2001**, she deposited in the United States Mail, Bismarck, North Dakota, **one** envelope with certified postage, return receipt requested, fully prepaid, securely sealed and each containing a photocopy of:

Order

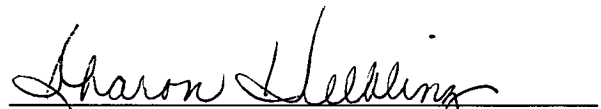
The envelope was addressed as follows:

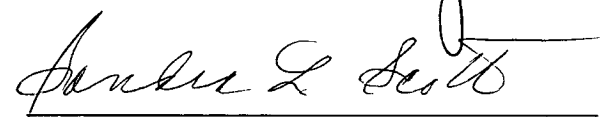
Monique Byrnes
Technologies Management Inc
P O Drawer 200
Winter Park FL 32790-0200
Cert. No. 7000 0520 0022 8654 0773

Each address shown is the respective addressee's last reasonably ascertainable post office address.

Subscribed and sworn to before me
this **15th day of March, 2001**.

SEAL





Notary Public





Public Service Commission
State of North Dakota

COMMISSIONERS

Susan E. Wefald, President
Leo M. Reinbold
Anthony T. Clark

Executive Secretary
Jon H. Mielke

600 E Boulevard Ave. Dept. 408
Bismarck, North Dakota 58505-0480
web: www.psc.state.nd.us
e-mail: sab@oracle.psc.state.nd.us
TDD 800-366-6888
Fax 701-328-2410
Phone 701-328-2400

March 15, 2001

Monique Byrnes
Technologies Management Inc
P O Drawer 200
Winter Park FL 32790-0200

Dear Ms. Byrnest:

On March 14, 2001, the Commission issued Certificate of Public Convenience and Necessity No. 4679 to Z-Tel Communications, Inc. to provide facilities-based local exchange telecommunications services throughout North Dakota, Case No. PU-2079-00-655. The original certificate is enclosed.

The Commission maintains a mailing list of telecommunications companies to which we mail notices relating to telecommunications issues. These notices are also published on the web site for your review ([HTTP://PC6.PSC.STATE.ND.US](http://PC6.PSC.STATE.ND.US) or [HTTP://WWW.STATE.ND.US](http://WWW.STATE.ND.US) (under "North Dakota State Government)).

In an effort to cut down on printing and mailing costs, I will **not** add this company to that list unless you request that I do so. You can contact me at 701-328-4076, FAX 701-328-2410, E-Mail msmail.sdh@oracle.psc.state.nd.us, or write.

Sincerely,

Sharon Helbling
Public Utilities Division

sdh

Enclosure

APPROVED

MOTION

DATE: 3-14-01
KMF March 14, 2001

**Z-Tel Communications, Inc.
Local Exchange
Public Convenience and Necessity**

Case No. PU-2079-00-655

I move the Commission adopt the Order and issue a Certificate of Public Convenience and Necessity to Z-Tel Communications, Inc. to provide local exchange telecommunications services throughout North Dakota, Case No. PU-2079-00-655.

JRL/sdh

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

Z-Tel Communications, Inc.
Local Exchange
Public Convenience and Necessity

Case No. PU-2079-00-655

ORDER

March 14, 2001

On December 5, 2000, Z-Tel Communications, Inc. (Z-Tel) filed an application for a certificate of public convenience and necessity to provide facilities-based local exchange telecommunications services throughout North Dakota.

Also on December 5, 2000, the Public Service Commission's Director of Accounting filed a memorandum indicating that Z-Tel has the financial ability to provide telecommunications service.

On December 20, 2000, the Commission issued a Notice of Opportunity for Hearing, which provided until January 25, 2001 for receiving comments or hearing requests. No requests for hearing were received. The Notice indicated the following issues to be considered in this matter:

1. Fitness and ability of the applicant to provide service.
2. Adequacy of the proposed service.
3. The technical, financial and managerial ability of the applicant to provide service.

On January 12, 2001, the Rural Telephone Company Group submitted comments requesting that any order granting the application include limitations to preserve the "rural safeguard" rights of rural companies under the Telcom Act, 47 U.S.C. 251(f).

Z-Tel is a wholly-owned subsidiary of Z-Tel Technologies, Inc. Both are Delaware corporations with headquarters at Tampa, FL. Z-Tel indicates that it currently provides long distance service nationwide and local exchange service to approximately 256,000 residential access lines in eleven states. Z-Tel further indicates that its management and key personnel have extensive telecommunications operational experience and technical expertise. The Commission finds Z-Tel is fit, able, and has the technical, financial and managerial ability to provide service.

Z-Tel states it is already operating as an interexchange carrier in North Dakota, where it is registered as a reseller of interexchange and local exchange services. Z-Tel plans to use ILEC unbundled network elements to begin offering services as soon as interconnection and resale arrangements are established. Z-Tel intends to offer local services as an adjunct to long distance. The Commission finds Z-Tel's proposed service adequate.

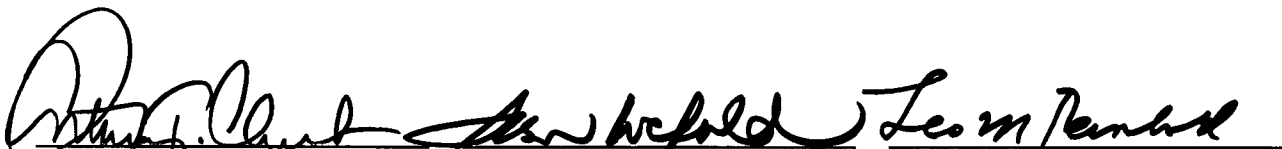
In this Case, as in other cases in which statewide authority was requested, the Commission will adhere to the precedent established in the AT&T certificate case, Case No. PU-453-96-83. In AT&T, the Commission held that its determination of the public interest with regard to the service territories of rural telephone companies is subject to any future proceedings under Section 251(f)(1) or (2) of the Telecommunications Act of 1996 (47 U.S.C. §251(f)(1) or (2)). The Commission also held that granting the certificate on a statewide basis is not a ruling that affects the rights of specific rural telephone companies under 47 U.S.C. §251(f).

Order

The Commission Orders:

1. The application of Z-Tel Communications, Inc. for a certificate of public convenience and necessity to provide facilities-based competitive local exchange services throughout North Dakota is GRANTED.
2. Granting Z-Tel a certificate to provide local exchange service on a statewide basis does not affect the rights of rural telephone companies under 47 U.S.C. §251(f).

PUBLIC SERVICE COMMISSION



Anthony T. Clark Susan E. Wefald Leo M. Reinbold
Commissioner President Commissioner

STATE OF NORTH DAKOTA

Certificate of Public Convenience and Necessity

Certificate Number 4679

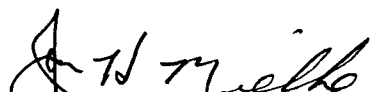
This is to certify that public convenience and necessity require, and permission is granted for Z-Tel Communications, Inc., a telecommunications public utility, to provide statewide local exchange telecommunications services, with facilities, in North Dakota.

This certificate is issued in Case No. PU-2079-00-655 and is conditioned upon Z-Tel Communications, Inc. securing the franchise or other authority of the proper municipal or other authority for the exercise of these rights and privileges.

Bismarck, North Dakota, March 14, 2001.

ATTEST:

PUBLIC SERVICE COMMISSION


Executive Secretary


Commissioner



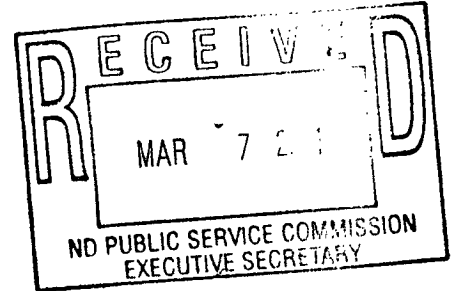
210 N. Park Ave.
Winter Park, FL
32789

P.O. Drawer 200
Winter Park, FL
32790-0200

Tel: 407-740-8575
Fax: 407-740-0613
tmi@tminc.com

March 6, 2001
Overnight Delivery

Mr. John Mielke
Executive Secretary
North Dakota Public Service Commission
State Capital
Bismarck, North Dakota 58505-0480



RE: Application of **Z-Tel Communications, Inc.** for a Certificate of Public Convenience and Necessity to Provide Facility-Based Local Telecommunications Services Within the State of North Dakota

Dear Mr. Mielke:

Enclosed for filing are the original and six (6) copies of an Affidavit provided at the request of Staff in the Application of Z-Tel Communications, Inc. for a Certificate of Public Convenience and Necessity to Provide Facility-Based Local Telecommunications Services Within the State of North Dakota.

Please acknowledge receipt of this application by date-stamping the extra copy of this cover letter and returning it to me in the self-addressed, stamped envelope provided for this purpose.

Any questions you may have regarding this filing may be directed to me at (407) 740-8575. Thank you for your assistance in this matter

Sincerely,

Monique Byrnes
Consultant to Z-Tel Communications, Inc.

cc: S. Byrne, Z-Tel
file: Z-Tel - ND local
tms: nd10000b

PU-2079-00-655

Pages: 2

Cover letter and Affidavit

by Z-Tel Communications, Inc.

03/07/2001

CC: Comm Legal Ilona Jerry

AFFIDAVIT

I, Timothy Seat, of lawful age, being duly sworn under oath depose and says as follows:

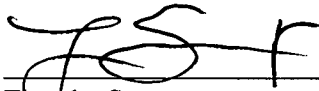
I am the Vice President - Regulatory Affairs for Z-Tel Communications, Inc., a Delaware Corporation; which is seeking a Certificate of Public Convenience and Necessity to provide local exchange services in the State of North Dakota.

I, as an authorized agent, and on behalf of Z-Tel Communications, Inc., attest that the Application by Z-Tel Communications, Inc. for a Certificate of Public Convenience and Necessity for Local Exchange Service is true in substance and in fact, except as to those matters stated upon information and belief, and as to those, I believe same to be true.

This Application demonstrates

- a) that Z-Tel possesses the technical, financial and managerial resources to provide local exchange service in North Dakota;
- b) the proposed services of Z-Tel are adequate and in fact provide an alternative service mix to consumers and
- c) Z-Tel is fit and able to provide service in North Dakota as successfully as it is so doing in its existing service area of seventeen (17) states.

Respectfully submitted on behalf of,
Z-Tel Communications, Inc.



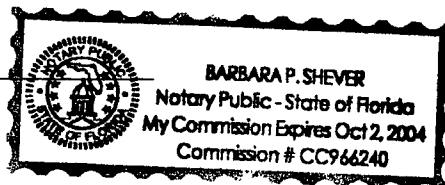
Timothy Seat
Vice President - Regulatory Affairs
Z-Tel Communications, Inc.

Subscribed and sworn to before me this 5th day of March, 2001



Notary Public

My commission expires: _____



INFORMAL AGENDA

February 21, 2001

PU-2079-00-655

Z-Tel Communications, Inc.
Local Exchange
Public Convenience and Necessity

Premiere

11

PU-2477-01-8

Pages: 1

Informal Hearing Held

by Public Service Commission

02/21/2001

CC: Comm Legal Ilona Jerry .

PU-2079-00-655

Pages: 1

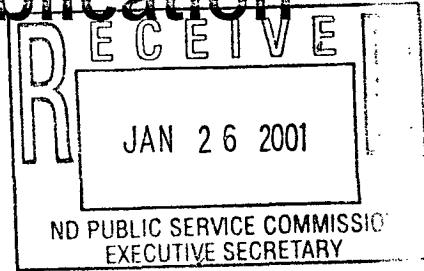
Informal Hearing Held

by Public Service Commission

02/21/2001

CC: Comm Legal Ilona Jerry .

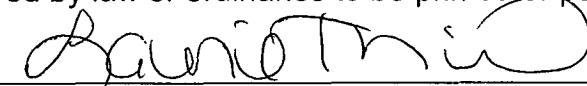
Affidavit of Publication



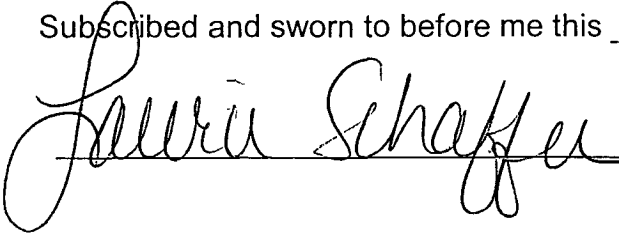
State of North Dakota)
)
County of Burleigh)

Laurie Thiel , being duly sworn, state as follows:

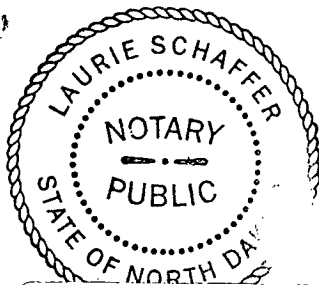
1. I am the designated agent, under the provisions and for the purposes of, Section 31-04-06, NDCC, for the newspapers listed on the attached exhibits.
2. The newspapers listed on the exhibits published the advertisement of:
2-Tel Comm , 1 time(s)
as required by law or ordinance.
3. All of the listed newspapers are legal newspapers in the State of North Dakota and, under the provisions of Section 46-05-01, NDCC, are qualified to publish any public notice or any matter required by law or ordinance to be printed or published in a newspaper in North Dakota.

Signed: 

Subscribed and sworn to before me this 10th day of January A.D. 2000.



LAURIE SCHAFFER
Notary Public, STATE OF NORTH DAKOTA
My Commission Expires DEC. 1, 2005



Notice of Opportunity For Hearing
December 20, 2000
Case No. PU-2079-00-655

Bismarck	12-27
Devils Lake	12-27
Dickinson	12-27
Fargo	1-2
Grand Forks	12-27
Jamestown	12-27
Minot	12-27
Valley City	12-27
Walpeton	12-31
Williston	12-27

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

Z-Tel Communications, Inc.
Local Exchange
Public Convenience & Necessity

Case No. PU-2079-00-655

AFFIDAVIT OF SERVICE BY ORDINARY MAIL OR E-MAIL

STATE OF NORTH DAKOTA
COUNTY OF BURLEIGH

Sharon Helbling deposes and says that:

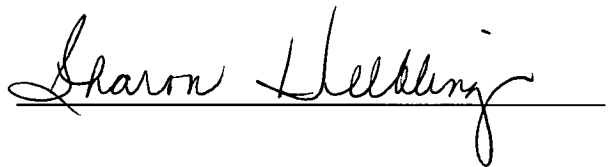
she is over the age of 18 years and not a party to this action and, on the **21st day of December, 2000**, she deposited in the United States Mail, Bismarck, North Dakota, envelopes by first class mail, fully prepaid, securely sealed, each containing a photocopy of:

Notice of Opportunity for Hearing


The envelopes were addressed as follows:

See Attached List

Each address shown is the respective addressee's last reasonably ascertainable post office address.



Subscribed and sworn to before me
this **21st day of December, 2000**.



Notary Public

SEAL

CHARLENE A. MAGSTADT
Notary Public, State of NORTH DAKOTA
My Commission Expires Jan. 7, 2004

wahlgren@rus.usda.gov
Wayne Ahlgren

bberkenpas@odusa.com
Barb Berkenpas

wbrudvik@ohnstadlaw.com
William Brudvik

donlee@martin-associates.com
Don Lee

jxpet23.uswest.com
Janis Peterson

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Lise Strom

harumiyamamoto@dwt.com
Harumi Yamamoto

ruth.holder@teligent.com
Ruth Holder

nlarsen@nvc.net
Clint Hanson
Accent Communications Inc
235 E 1st Ave
Groton SD 57445

jlchapman@acomminc.com
Jerry Chapman
Acomm Inc
510 1st Ave N Ste 203
Minneapolis MN 55403-0343

smassey@bepc.com
Sheryl Massey
Basin Electric Power Coop
1717 E Interstate Ave
Bismarck ND 58501-0564

jtmgr@bektel.com
Jerome Tishmack
BEK Communications Cooperative
PO Box 230
Steele ND 58482-0230

jtmgr@bektel.com
Jerome Tishmack
BEK Communications I Inc
PO Box 230
Steele ND 58482-0230

ken@staff.ctctel.com
L Dan Wilhelmson
Consolidated Comm Networks Inc
PO Box 1077
Dickinson ND 58601-1077

ken@staff.ctctel.com
L Dan Wilhelmson
Consolidated Telcom Inc
PO Box 1077
Dickinson ND 58601-1077

ken@staff.ctctel.com
L Dan Wilhelmson
Consolidated Telephone Cooperative
PO Box 1077
Dickinson ND 58601-1077

drtc@drtel.net
Darren Moser
Dickey Rural Telephone Cooperative
PO Box 69
Ellendale ND 58436-0069

glenn.richards@shawpittman.com
Glenn Richards
Glenn Richards
ShawPittman
2300 N St NW

rlaqua@rrv.net
Ronald Laqua
Halstad Telephone Company
PO Box 55
Halstad MN 56548-0055

dclark@hq.idt.net
Diane Clark
IDT America, Corp.
520 Broad St 7th Fl
Newark NJ 07102

kander@ictc.com
Keith Anderson
Inter-Community Telephone Co. II
PO Box 8
Nome ND 58062-0008

nschmid@acginc.net
Neil Schmid
Ionex Communications North Inc
5710 LBJ Frwy Ste 215
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Scobey MT 59263

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Rochester MI 48307-1837

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Doris Cooper
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Blue Bell PA 19422

Tele-Tech Inc
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Sioux Falls SD 57104-3660

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Hazen ND 58545-0467

Western CLEC Corporation
3650 131st Ave SE #400
Bellevue WA 98006

Z-Tel Communications Inc
601 S Harbour Island Blvd Ste 220
Tampa FL 33602-5925

PU-2079-00-655

Copies To:

State Library (8 copies)

Historical Society

Associated Press

Helbling, Sharon D.
From: Helbling, Sharon D.
Sent: Thursday, December 21, 2000 9:02 AM
To: ndna (E-mail)
Subject: Attached Notice of Opportunity for Hearing and Notice of Opportunity to File Written Comments



1.doc



1.doc

Please have the attached Notices published as legal publications in the next issue of the ten North Dakota daily newspapers, and run them as "News Item Only" articles as well.

Send the bill to the Public Service Commission along with a tear sheet for billing purposes. If you have any questions, please call me at 328-4076.

Thank you.

Sharon Helbling
Public Utilities Division

MOTION

December 20, 2000

APPROVED:

DATE: 12-20-00
KMF

**Z-Tel Communications, Inc.
Local Exchange
Public Convenience and Necessity**

Case No. PU-2079-00-655

I move the Commission issue a Notice of Opportunity for Hearing in the application of Z-Tel Communications, Inc. for a Certificate of Public Convenience and Necessity to provide local exchange telecommunications services throughout North Dakota, Case No. PU-2079-00-655.

JRL/sdh

000655-2.doc

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

Z-Tel Communications, Inc.
Local Exchange
Public Convenience and Necessity

Case No. PU-2079-00-655

NOTICE OF OPPORTUNITY FOR HEARING

December 20, 2000

On December 5, 2000, Z-Tel Communications, Inc. of Tampa, Florida filed an application for a certificate of public convenience and necessity to provide facilities-based local exchange telecommunications services throughout North Dakota.

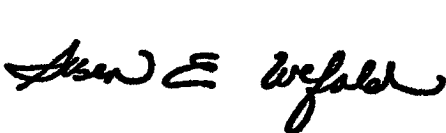
The issues to be considered in this matter are:

1. Fitness and ability of the applicant to provide service.
2. Adequacy of the proposed service.
3. The technical, financial and managerial ability of the applicant to provide service.

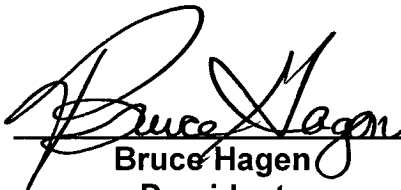
Those interested are invited to comment on this application in writing. Persons desiring a hearing must file a written request identifying their interest in the proceeding and the reasons for requesting a hearing. Comments and requests for hearings must be received by **January 25, 2001**. If deemed appropriate, the Commission can determine the matter without hearing.

For more information contact the Public Service Commission, State Capitol, Bismarck, North Dakota 58505, 701-328-2400; or Relay North Dakota 1-800-366-6888 TTY. If you require any auxiliary aids or services, such as readers, signers, or Braille materials please notify Jon Mielke, Executive Secretary.

PUBLIC SERVICE COMMISSION



Susan E. Wefald
Commissioner



Bruce Hagen
President



Leo M. Reinbold
Commissioner

STATE OF NORTH DAKOTA
PUBLIC SERVICE COMMISSION

Z-Tel Communications Inc.
Local Exchange
Public Convenience and Necessity

Case No. PU-1544-00-655

AFFIDAVIT OF SERVICE BY CERTIFIED MAIL

STATE OF NORTH DAKOTA
COUNTY OF BURLEIGH

Sharon Helbling deposes and says that:

she is over the age of 18 years and not a party to this action and, on the **5th day of December, 2000**, she deposited in the United States Mail, Bismarck, North Dakota, **one** envelope with certified postage, return receipt requested, fully prepaid, securely sealed and each containing a photocopy of:

Staff Memorandum on Financial Ability

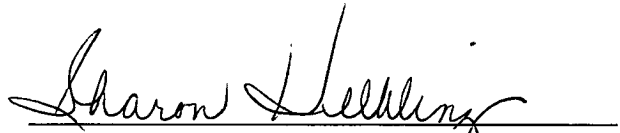
The envelope was addressed as follows:


Monique Byrnes
Technologies Management Inc
P O Drawer 200
Winter Park FL 32790-
Cert. No. 7000 0520 0022 8653 3034

Each address shown is the respective addressee's last reasonably ascertainable post office address.

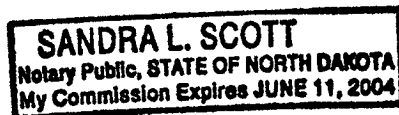
Subscribed and sworn to before me
this **5th day of December, 2000**.

SEAL





Notary Public





Public Service Commission
State of North Dakota

Memorandum

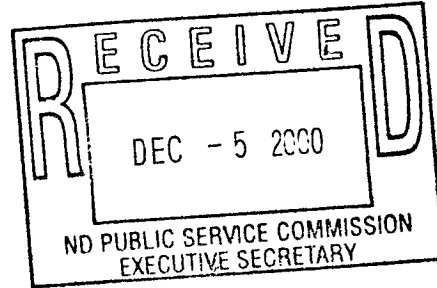
600 E Boulevard Ave. Dept. 408
Bismarck, North Dakota 58505-0480
e-mail: msmail.sab@oracle.psc.state.nd.us
TDD 800-366-6888
Fax 701-328-2410
Phone 701-328-2400

COMMISSIONERS

Bruce Hagen
President
Susan E. Wefald
Leo M. Reinbold

To: Jon Mielke
From: Mike Diller *Mike Diller*
Date: December 5, 2000
Re: **Z-Tel Communications, Inc.
Local Exchange PC&N
Case No. PU-2079-00-655**

Executive Secretary
Jon H. Mielke



The following is written to provide the commission with a very limited review of this case regarding the financial ability of the applicant to provide local exchange service in North Dakota.

Z-Tel Technologies, Inc., wholly owns the applicant and is a public company traded on the NASDAQ. According to financial information provided for the year ended 1999, Z-Tel Technologies, Inc. has sufficient equity to provide financial support to Z-Tel Communications for the purpose of providing local exchange service in North Dakota.

The Telecommunications Act of 1996 established a national policy to create a competitive environment for telephone service. The applicant is one of many companies responding to the Act.

I see no reason to deny the applicant's request.

In accordance with the Commission's wishes, I have served this document on the applicant.



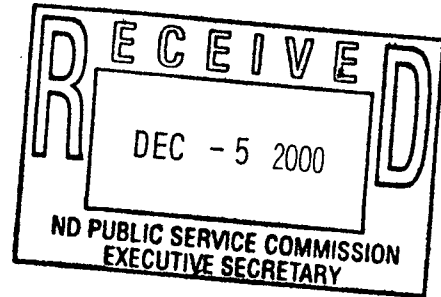
210 N. Park Ave.
Winter Park, FL
32789

P.O. Drawer 200
Winter Park, FL
32790-0200

Tel: 407-740-8575
Fax: 407-740-0613
tmi@tminc.com

December 4, 2000
Overnight Delivery

Mr. John Mielke
Executive Secretary
North Dakota Public Service Commission
State Capital
Bismarck, North Dakota 58505-0480



RE: Application of **Z-Tel Communications, Inc.** for a Certificate of Public Convenience and Necessity to Provide Facility-Based Local Telecommunications Services Within the State of North Dakota

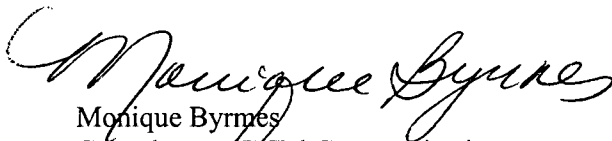
Dear Mr. Mielke:

Enclosed for filing are the original and six (6) copies of the Certificate of Good Standing from the Secretary of the State of North Dakota to accompany the application of Z-Tel Communications, Inc. for a Certificate of Public Convenience and Necessity to Provide Facility-Based Local Telecommunications Services Within the State of North Dakota.

Please acknowledge receipt of this application by date-stamping the extra copy of this cover letter and returning it to me in the self-addressed, stamped envelope provided for this purpose.

Any questions you may have regarding this filing may be directed to me at (407) 740-8575. Thank you for your assistance in this matter

Sincerely,


Monique Byrnes
Consultant to Z-Tel Communications, Inc.

cc: S. Greenhawt, Z-Tel
file: Z-Tel - ND local
tms: ndl0000a

1 **PU-2079-00-655**

Pages: 139

Application for Local Exchange PC&N

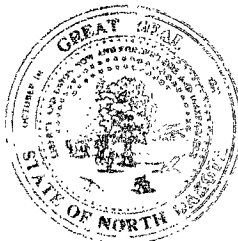
by Z-Tel Communications, Inc.

12/05/2000

CC: Comm Legal Ilona Jerry .

State of North Dakota

SECRETARY OF STATE



CERTIFICATE OF GOOD STANDING

OF

Z-TEL COMMUNICATIONS, INC.

The undersigned, as Secretary of State of the State of North Dakota, hereby certifies that Z-TEL COMMUNICATIONS, INC., a Delaware corporation, authorized to transact business in the State of North Dakota on June 23, 1998, and according to the records of this office as of this date, has paid all fees due this office as required by North Dakota statutes governing foreign corporations.

ACCORDINGLY the undersigned, as such Secretary of State, and by virtue of the authority vested in him by law, hereby issues this Certificate of Good Standing to

Z-TEL COMMUNICATIONS, INC.

Issued: November 28, 2000

A handwritten signature in cursive script, reading "Alvin A. Jaeger".

Alvin A. Jaeger
Secretary of State



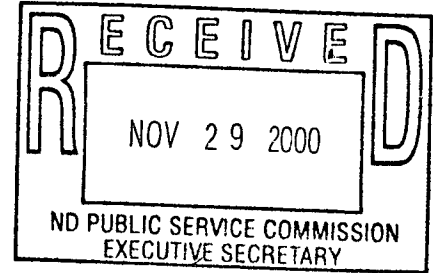
210 N. Park Ave.
Winter Park, FL
32789

P.O. Drawer 200
Winter Park, FL
32790-0200

Tel: 407-740-8575
Fax: 407-740-0613
tmi@tminc.com

November 28, 2000
Overnight Delivery

Mr. John Mielke
Executive Secretary
North Dakota Public Service Commission
State Capital
Bismarck, North Dakota 58505-0480



RE: **Application of Z-Tel Communications, Inc.** for a Certificate of Public Convenience and Necessity to Provide Facility-Based Local Telecommunications Services Within the State of North Dakota

Dear Mr. Mielke:

Enclosed for filing are the original and six (6) copies of the application of Z-Tel Communications, Inc. for a Certificate of Public Convenience and Necessity to provide facility-based local exchange services within the State of North Dakota. An original Certificate of Good Standing from the Secretary of the State of North Dakota will be filed under separate cover.

Please acknowledge receipt of this application by date-stamping the extra copy of this cover letter and returning it to me in the self-addressed, stamped envelope provided for this purpose.

Any questions you may have regarding this filing may be directed to me at (407) 740-8575. Thank you for your assistance in this matter

Sincerely,


Monique Byrnes
Consultant to Z-Tel Communications, Inc.

cc: S. Greenhawt, Z-Tel
file: Z-Tel - ND local
tms: nd10000

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF NORTH DAKOTA**

In the Matter of the Application of)
Z-Tel Communications, Inc.) Case No. _____
To Provide Facilities-based Local)
Exchange Service Throughout)
The State of North Dakota)

**APPLICATION FOR CERTIFICATE OF PUBLIC
CONVENIENCE AND NECESSITY TO PROVIDE
FACILITIES-BASED LOCAL TELECOMMUNICATIONS SERVICES**

Application is hereby made to Public Service Commission of the State of North Dakota (the "Commission") by Z-Tel Communications, Inc. ("Applicant" or "Z-Tel") for a Certificate of Public Convenience and Necessity to provide telecommunications service in the State of North Dakota, pursuant to NDCC Sections 49-03.01 et seq. and 69-02-04 of the Commission's Rules of Practice and Procedure. Z-Tel proposes to offer facility-based local telecommunications services throughout the state in conjunction with other local and long distance services offered on a resale basis.

Applicant has received authority from the Commission to operate as a reseller of long distance and local exchange telecommunications services in North Dakota, Case No. PU-2079-99-150, under Certificate of Registration Nos. 620 and 621 respectively. Applicant now requests facilities-based local exchange authority in addition to the authority previously granted.

In support of its Application, Z-Tel submits the following:

1. Introduction

Z-Tel is requesting authority to provide basic facilities-based local exchange service to both residence and business customers throughout North Dakota in all exchanges which are not exempt from competition. The services that Z-Tel intends to offer will be an adjunct to the long distance services that the company has previously received authority to provide statewide. Z-Tel plans to offer service via an unbundled network element platform (UNE-P) through interconnection agreements with incumbent local exchange carriers ("LECs"). Should its Application be granted, Z-Tel plans to commence offering service immediately upon the establishment of the appropriate and necessary resale arrangements with the incumbent LECs.

II. Description of the Applicant

- (a) Z-Tel Communications, Inc. is incorporated in the State of Delaware. The main address of the corporation is:

Z-Tel Communications, Inc.
601 South Harbour Island Boulevard, Suite 220
Tampa, Florida 33602
Telephone: (813) 233-4611
Facsimile: (813) 233-4620
Toll Free: (800) 511-4572

- (b) All correspondence, notices, inquiries and other communications regarding this Application should be addressed to:

Monique Byrnes
Technologies Management, Inc.
P.O. Box 200
Winter Park, Florida 32789
Telephone: (407) 740-8575
Facsimile: (407) 740-0613

- (c) The Applicant is a Delaware Corporation, authorized by the North Dakota Secretary of State to transact business in the State of North Dakota.
- (d) Z-Tel is a telecommunications company that has been providing long distance services nationwide and local exchange services in the following states: California, Georgia, Illinois, Maryland, Massachusetts, Michigan, New York, Oregon, Pennsylvania, Texas and Washington.

III. Exhibits

In support of this Application, the following exhibits are attached hereto:

- Exhibit A - Certificate of Incorporation
- Exhibit B - Certificate of Authority to Transact Business in the State of North Dakota;
- Exhibit C - Financial Statements
- Exhibit D - Profiles of Senior Management Key Personnel
- Exhibit E - Press Release
- Exhibit F - Service Area Map
- Exhibit G - Carriers Offering Similar Services

IV. Financial, Technical and Managerial Qualifications

Z-Tel possesses the managerial, technical and financial ability to provide local telecommunications service in the State of North Dakota. Z-Tel has strong financial resources to enable the company to successfully provide local telecommunications service in the State of North Dakota. Z-Tel is in the process of obtaining approval to provide local service to customers in numerous states.

IV.A. Financial Qualifications

- (a) By utilizing its current customer service, operations, management, and technical workforce and infrastructure supporting its facilities-based local exchange and interexchange operations, Z-Tel is financially and otherwise capable and qualified to offer and maintain all of its tariffed services in its territories served through via its own and/or through the underlying carrier's facilities.
- (b) The costs of North Dakota operations will consist of leasing UNE-P and additional administrative and sales overhead. Z-Tel is already operating as an interexchange carrier in North Dakota and is operating as a facilities-based local exchange service provider in several states. The incremental administrative and sales costs are not projected to be significant for the company. No new funds or capital will be required to expand the company's services in North Dakota.
- (c) Z-Tel provides the financial statements of its parent company, Z-Tel Technologies, Inc., a public company traded on the NASDAQ, as proof of its financial stability to provide the required services within the State of North Dakota as Exhibit C.

IV.B. Managerial Qualifications

- (a) Z-Tel possesses managerial qualifications to operate a Competitive Local Exchange Carrier within the State of North Dakota. Biographical summaries of the managerial experience of Z-Tel and its parent company are found in Exhibit D.

IV.C. Technical Qualifications

- (a) Z-Tel's services will satisfy the minimum standards established by the Commission. The Company will file and maintain tariffs in the same manner and form as required of incumbent local exchange telecommunications companies with which Z-Tel seeks to compete.

- (b) Z-Tel has experience operating as a local exchange providers in several states. The company has in excess of 256,000 residential local exchange access line subscribers. As the foregoing illustrates, Z-Tel possesses considerable telecommunications expertise. Please See Exhibit E for a Press Release on this issue. Based on the company's experience and proven track record, Z-Tel is certainly technically qualified to provide local exchange service in North Dakota.

V. Customer Service

Z-Tel understands the importance of effective customer service for local service consumers. Z-Tel has a toll free customer service telephone number that is available with live operator response 24 hours per day, 7 days per week. Z-Tel's toll free telephone number for customer inquiries, complaints and repair is 1-800-511-4572. In addition, customers may contact the company in writing at the headquarters address.

The contact for resolution of customer complaints with the Commission is:

Linda Farr
Manager, Regulatory Affairs
Z-Tel Communications, Inc.
100 Brookwood Road
Atmore, AL 36504
334-446-2502

VI. Service Description

Z-Tel proposes to provide facilities-based local exchange services via an unbundled network element platform (UNE-P). The company intends to offer service immediately upon certification and approval of its interconnection agreement.

Z-Tel's primary market is residential customers. Z-Tel intends to provide a network bundled telecommunications service which would include long distance service, local exchange service, voice mail and selected custom calling features. In addition, the Company will provide to its customers additional custom calling and CLASS features, access to emergency call services (e.g. 911), directory assistance and other ancillary services.

Z-Tel intends to offer service in the geographic areas currently served by Qwest Corporation. Z-Tel will mirror the basic local calling scopes of the incumbent local exchange companies.

Z-Tel will provide Customers with access to 911 and E911 emergency services where available, and will cooperate with existing telecommunications companies, and other affected agencies and organizations, to arrange for the necessary interconnections to enable efficient completion of these calls.

Upon granting of a Certificate of Public Convenience and Necessity and approval of an interconnection agreement, Z-Tel will file a tariff with the Commission containing descriptions and rates for its facility-based and resale local exchange services.

VII. Public Interest Standard

Grant of Z-Tel's Application to provide facilities-based local exchange services is in the public interest and serves the public convenience and necessity. In enacting the Federal Telecommunications Act of 1996, the United States Congress determined that it is in the public interest to promote competition in the provision of telecommunications services, including local exchange services. Experience with competition in other telecommunications markets, such as long distance, competitive access, and customer premises equipment, demonstrates the benefits that competition can bring to consumers. Consumers are enjoying increased services, lower prices, higher quality, and greater reliability. This is true not only with respect to the service offerings of the new entrants, but also as a result of the response of incumbent monopoly providers to the introduction of competition.

Most competition in the local exchange market has been for business customers. Z-Tel plans to bring the benefits of competition to residential consumers. Z-Tel's proposed services will provide multiple public benefits by increasing the competitive choices available to users in North Dakota. Enhanced competition in telecommunications services likely will further stimulate economic development in North Dakota. In addition, increased competition will create incentives for all carriers to offer lower prices, more innovative services, and more responsive customer service.

VIII. Waivers and Regulatory Compliance

Z-Tel has reviewed all of the Commission's rules applicable to competitive local exchange service providers and agrees to comply with those rules except to the extent the rules are explicitly waived for Z-Tel or for all carriers in the same class. Specifically, Z-Tel requests exemption from the following rules:

- (a) Title 41, Chapter 1, Rules 101-103.02 - Guarantee in lieu of deposit: Z-Tel requests exemption only from that portion of the rule that requires a guarantee form on file with the Commission.
- (b) Title 41, Chapter 1, Rule 502.01 - Service Standards: To the extent that Z-Tel offers service on a UNE-P and resold basis from the incumbent local exchange service providers, Z-Tel requests a waiver of the requirement to adopt and pursue a maintenance program for outside plant facilities and equipment.

- (c) Title 41, Chapter 2, Rule 102.03 - Press Release: Z-Tel requests a waiver of the requirement to send a press release to all newspapers, radio and television stations on the Commission's list. Unlike the incumbent LECs whose customer density in any given area makes press releases practical, Z-Tel does not anticipate sufficient market share to warrant the expense of preparing and coordinating a press release. Z-Tel maintains a detailed web site which includes information on the company's services and rates as well as corporate information and all press releases. Z-Tel customers will be informed of the company's web site and will be able to receive all manner of information from that cite. In addition, consumers will be informed of rate increases by bill insert. Therefore, the additional step of notification via press release is unnecessary.
- (d) Local Exchange Directories: Z-Tel requests that it not be required to publish local exchange directories. Z-Tel will make arrangements with the incumbent LECs whereby the names of Z-Tel's customers will be included in the directories published by the incumbent LECs. These directories will be distributed to Z-Tel's customers. This approach is entirely reasonable and will have a direct benefit to the customers of both Z-Tel and the incumbent LECs since customers will have to refer to only one directory for a universal listing of customer information. It would be an unnecessary burden on Z-Tel to require that it publish and distribute its own directory to all customers located within each exchange area, particularly since nearly all of these customers will be customers of the incumbent LECs. It is more efficient for Z-Tel to simply include its limited customer list in the existing directories of the incumbent LECs.
- (e) Reporting Requirements: Z-Tel further requests waivers of any reporting requirements which, although applicable to incumbent LECs, are not applicable to competitive providers such as Z-Tel because such requirements: (1) are not consistent with the demands of the competitive market; and (2) they constitute an undue burden on a competitive provider, thereby requiring an inefficient allocation of its limited resources. In addition, Z-Tel reserves the right to seek any regulatory waivers which may be required for Z-Tel to compete effectively in the North Dakota local exchange services market.

VIII. Conclusion

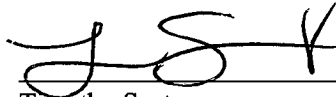
This Application demonstrates that Z-Tel possesses the technical, financial and managerial resources to provide local exchange service in North Dakota.

Wherefore, Z-Tel respectfully requests that the Commission:

1. grant Z-Tel authority to operate as a provider of basic local exchange telecommunications services in the State of North Dakota;
2. grant the waivers requested in this Application; and
3. grant such other relief as it deems necessary and appropriate.

Respectfully submitted,

Z-Tel Communications, Inc.



Timothy Seat

Vice President - Regulatory Affairs

Z-Tel Communications, Inc.

777 South Harbour Island Boulevard, Suite 990

Tampa, Florida 33602

Telephone: (813) 233-4611

Facsimile: (813) 233-4620

VERIFICATION

STATE OF FLORIDA

COUNTY OF HILLSBOROUGH

Timothy Seat, being first duly sworn, deposes and says: That he is the Vice President - Regulatory Affairs for Z-Tel Communications, Inc. the Applicant in the foregoing Application; that he has read the foregoing Application, knows the contents thereof and is authorized to verify the accuracy of same; and that the statements contained in the Application are true to his best knowledge, information and belief.

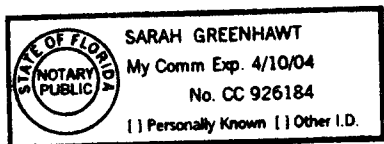


Timothy Seat
Vice President - Regulatory Affairs
Z-Tel Communications, Inc.
777 South Harbour Island Boulevard, Suite 990
Tampa, Florida 33602
Telephone: (813) 233-4611
Facsimile: (813) 233-4620

Subscribed and sworn to before me this 16 day of November, 2000.



Notary Public



My commission expires: 4/10/04

Z-TEL COMMUNICATIONS, INC

Exhibit A

Certificate of Incorporation

State of Delaware
Office of the Secretary of State PAGE 1

I, EDWARD J. FREEL, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY THE ATTACHED IS A TRUE AND CORRECT COPY OF THE RESTATED CERTIFICATE OF "Z-TEL TECHNOLOGIES, INC.", CHANGING ITS NAME FROM "Z-TEL TECHNOLOGIES, INC." TO "Z-TEL COMMUNICATIONS, INC.", FILED IN THIS OFFICE ON THE SECOND DAY OF APRIL, A.D. 1998, AT 4:30 O'CLOCK P.M.



Edward J. Freel

Edward J. Freel, Secretary of State

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AUTHENTICATION: 9010968

DATE: 04-03-98

**RESTATED CERTIFICATE OF INCORPORATION
OF
Z-TEL TECHNOLOGIES, INC.**

Z-Tel Technologies, Inc., a corporation organized and existing under the laws of the State of Delaware, hereby certifies as follows:

The name of the corporation is Z-Tel Technologies, Inc. The date of filing of its original Certificate of Incorporation with the Secretary of State was January 15, 1998, under the name Olympus Telecommunications Group, Inc.

The text of the Certificate of Incorporation as amended or supplemented heretofore is further amended hereby to read as herein set forth in full:

1. The name of the corporation is Z-Tel Communications, 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 nature of the business or purposes to be conducted or promoted is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of Delaware.
4. The total number of shares of stock which the corporation shall have authority to issue is One Thousand (1,000) and the par value of each of such shares is Zero Dollars and One Cent (\$.01) amounting in the aggregate to Ten Dollars and No Cents (\$10.00).
5. The board of directors is authorized to make, alter or repeal the bylaws of the corporation. Election of directors need not be by written ballot.
6. The name and mailing address of the sole incorporator is:

Laura Vitalo
Corporation Trust Center
1209 Orange Street
Wilmington, Delaware 19801

7. 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

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Z-TEL TECHNOLOGIES

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Z-TEL TECHNOLOGIES

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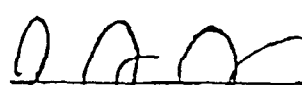
a knowing violation of law, (lii) under Section 174 of the Delaware General Corporation Law, or (iv) for any transaction from which the director derived an improper personal benefit.

8. The corporation shall indemnify its officers, directors, employees and agents to the extent permitted by the General Corporation Law of Delaware.

This Restated Certificate of Incorporation was duly adopted by the Board of Directors in accordance with Sections 241 and 245 of the General Corporation Law of the State of Delaware. The corporation has not received payment for its capital.

This Restated Certificate of Incorporation shall be effective on April 2, 1998.

IN WITNESS WHEREOF, said Z-Tel Technologies, Inc. has caused this Certificate to be signed by D. Gregory Smith, its president, this 2nd day of April, 1998.


D. Gregory Smith, President

Z-TEL COMMUNICATIONS, INC

Exhibit B

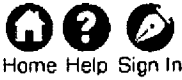
Certificate of Authority to Transact Business in the State of North Dakota

To be filed under separate cover.

Z-TEL COMMUNICATIONS, INC

Exhibit C

Financial Statements



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[Overview](#) Z-Tel Technologies Inc. (ticker: ZTEL, exchange: NASDAQ) News Release - 2-Nov-2000

[Z-Tel](#)

[Management Team](#)

[Stock Quote](#)

[Stock Chart](#)

[Fundamentals](#)

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Z-Tel Reports Record Operating Results and Sequentially Improved EBITDA for Third Quarter

TAMPA, Fla.--(BUSINESS WIRE)--Nov. 2, 2000--

EBITDA Makes Positive Turn As Higher Volumes, Improved Operating Margins and Efficiencies Begin to Leverage Core Overhead Sharply Increased Revenues, Gross Margin, Normalized EPS and Subscriber Count All Meet or Exceed Consensus Estimates

- Subscriber Count Grows 51% From Second Quarter to 256,000
- Revenues Increased 36% Sequentially Over Second Quarter 2000 to \$54 Million
- Fourth Consecutive Quarterly Gross Margin Increase, to 39%
- Five New State Markets, Doubling Addressable Market to 44 Million Potential Subscribers
- \$156 Million in New Funding Agreements Announced

Gregg Smith, President and Chief Executive Officer of Z-Tel Technologies, Inc. (Nasdaq/NMS:ZTEL), today announced better-than-expected financial results for the third quarter and nine months ended September 30, 2000.

Mr. Smith commented, "Z-Tel delivered strong financial results in the third quarter as we continued to add record numbers of subscribers and attain greater efficiencies throughout the organization. While Z-Tel is one of the fastest growing consumer communications companies, we have been able to simultaneously improve gross profit margins and other key operating metrics. We believe we are well positioned from a sales and marketing, operations and financial standpoint to continue growing and to reach positive EBITDA during the first half of 2001."

For the third quarter, Z-Tel's revenues were \$54,415,000, up 36% sequentially over \$40,157,000 for the second quarter of 2000. Z-Tel had negative EBITDA for the third quarter of \$15,920,000, a 13% sequential improvement from negative \$18,283,000 for the second quarter of 2000. The Company's loss for the third quarter, excluding beneficial conversion and warrant accretion related to the issuance of Series D preferred stock, was \$22,978,000, or \$0.69 per share, compared with a loss of \$23,055,000, or \$0.70 per share, for the second quarter of 2000.

Revenues increased to \$108,548,000 for the first nine months of 2000 from \$2,170,000 for the first nine months of 1999. Excluding the beneficial conversion and warrant accretion charges related to the issuance of Series D preferred stock, the company's loss was \$61,509,000, or \$1.87 per share, for the first nine months versus a loss of \$24,621,000, or \$1.71 per share, for the comparable prior-year

period.

Mr. Smith continued, "We are very pleased with subscriber and revenue growth, but the real story this quarter is the new efficiency that we are seeing in our operations. We also have continued to expand the market available to Z-Tel by entering five new states since the beginning of the third quarter - Georgia, Maryland, Oregon, California and Illinois - which has doubled our potential market to 44 million subscribers from 22 million. We also continue to improve the functionality of Z-Line's unique bundle of service with the recent addition of Z-Alerts(TM) and our new City of America(TM) service announced today. We are also planning to broaden our market geographically by entering additional states during the fourth quarter and early 2001."

Mr. Smith concluded, "We are also quite pleased with the confidence expressed by the financial community during the past four months as we raised \$156 million in new financing or funding commitments in a challenging market. In addition to a \$56 million preferred stock round announced in July 2000, we also closed or received commitments on a \$50 million receivables funding facility and announced an agreement regarding a \$50 million preferred stock investment by a Brown Brothers Harriman managed fund. We believe we are well positioned to continue our growth in the quarters ahead."

Z-Tel Technologies will hold a conference call to discuss this release today at 10:00 a.m. Eastern time. Investors will have the opportunity to listen to the conference call over the Internet by going to www.z-tel.com and clicking Investor Relations or by going to the following web sites - www.streetevents.com or www.vcall.com - at least fifteen minutes early to register, download, and install any necessary audio software. For those who cannot listen to the live broadcast, a replay will be available at these sites shortly after the call through the end of business on December 2, 2000.

About Z-Tel Technologies, Inc.(TM)

Z-Tel Technologies, Inc. provides consumers bundled local and long distance telephone services, combined with enhanced, Internet-based communications features that enable them to manage all of their voice communications needs. Z-Tel currently sells this bundle as "Z-Line Home Edition(TM)" in New York, Texas, Pennsylvania, Massachusetts, Georgia, Maryland, Oregon, California and Illinois, and has over 256,000 active customers. For more information about this innovative new service or about Z-Tel, please visit the Company's web site at www.z-tel.com.

Z-Tel Technologies, Inc., Z-Line, Z-Line Home Edition, Z-Alerts and City of America are trademarks of Z-Tel Technologies, Inc.

This press release contains forward-looking statements that are based upon current expectations and involve a number of risks and uncertainties. In order for Z-Tel to utilize the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, you are hereby cautioned, and Z-Tel hereby notes, that these statements may be affected by the risk that favorable growth and financial trends may not continue, the risk that the Company may not achieve positive EBITDA in the anticipated time frame or at all, the risk that the Company will be unable to efficiently and successfully enter new markets, the risk that the financings and other commitments described in this press release that have not yet closed are subject to closing conditions, and that if any of these conditions is not met, the financings and other commitments may not be completed; the risk that the anticipated efficiencies and reduction in expenses from the use of an electronic gateway will not be achieved in the time frame expected or at all; the risk that

unbundled network elements will cease to be available in their present form in states that have adopted favorable pricing rules for such elements and the risk that additional state regulatory commissions will not adopt favorable pricing rules for unbundled network elements, the risk that the Company's existing financing will not be sufficient to fund anticipated growth and that additional financing may not be available on favorable terms or at all, as well as the risk factors described in detail in Z-Tel's 1999 Annual Report on Form 10-K, filed March 28, 2000; and in Z-Tel's other filings with the Securities and Exchange Commission. Z-Tel undertakes no obligation to update or revise any such forward-looking statements.

Z-TEL TECHNOLOGIES, INC.
Unaudited Financial Highlights
(In thousands, except share and per share data)

	Three Months Ended September 30,	
	2000	1999
Revenues	\$ 54,415	\$ 745
EBITDA	\$ (15,920)	\$ (9,764)
Net loss	\$ (22,109)	\$ (12,097)
Net loss attributable to common stockholders	\$ (30,724)	\$ (12,465)
Basic and diluted loss per share	\$ (0.92)	\$ (0.96)
Weighted average common shares outstanding	33,536,724	13,025,563

	Nine Months Ended September 30,	
	2000	1999
Revenues	\$ 108,548	\$ 2,170
EBITDA	\$ (48,636)	\$ (18,431)
Net loss	\$ (60,640)	\$ (23,647)
Net loss attributable to common stockholders	\$ (69,255)	\$ (24,621)
Basic and diluted loss per share	\$ (2.11)	\$ (1.71)
Weighted average common shares outstanding	32,847,855	14,383,338

Z-Tel Technologies, Inc. and Subsidiaries
Condensed Consolidated Statements of Operations
(In thousands, except share and per share data)
(Unaudited)

	Three Months Ended September 30,	
	2000	1999
Revenues	\$ 54,415	\$ 745
Operating expenses:		
Network operations	33,032	2,039
Sales and marketing	11,742	2,112

Research and development	2,132	1,154
General and administrative	23,429	5,204
Depreciation and amortization	5,308	1,085
	-----	-----
Total operating expenses	75,643	11,594
	-----	-----
Operating loss	(21,228)	(10,849)
	-----	-----
Nonoperating income (expense):		
Interest and other income	736	87
Interest and other expense	(1,617)	(1,335)
	-----	-----
Total nonoperating income (expense)	(881)	(1,248)
	-----	-----
Net loss	(22,109)	(12,097)
Less mandatorily convertible redeemable preferred stock dividends and warrant accretion	(1,257)	(368)
Less beneficial conversion feature charge	(7,358)	--
	-----	-----
Net loss attributable to common stockholders	(30,724)	\$ (12,465)
	=====	=====
Weighted average common shares outstanding	33,536,724	13,025,563
	=====	=====
Basic and diluted net loss per share	\$ (.92)	\$ (.96)
	=====	=====
EBITDA	(15,920)	(9,764)
	=====	=====

	Nine Months Ended September 30,	
	2000	1999
	-----	-----
Revenues	\$ 108,548	\$ 2,170
	-----	-----
Operating expenses:		
Network operations	67,999	3,831
Sales and marketing	29,196	3,960
Research and development	5,221	2,619
General and administrative	54,768	10,191
Depreciation and amortization	11,800	2,749
	-----	-----
Total operating expenses	168,984	23,350
	-----	-----
Operating loss	(60,436)	(21,180)
	-----	-----
Nonoperating income (expense):		
Interest and other income	2,477	319
Interest and other expense	(2,681)	(2,786)
	-----	-----
Total nonoperating income (expense)	(204)	(2,467)
	-----	-----
Net loss	(60,640)	(23,647)
Less mandatorily convertible		

redeemable preferred stock		
dividends and warrant accretion	(1,257)	(974)
Less beneficial conversion feature charge	(7,358)	--
	-----	-----
Net loss attributable to common stockholders	\$ (69,255)	\$ (24,621)
	=====	=====
Weighted average common shares outstanding	32,847,855	14,383,338
	=====	=====
Basic and diluted net loss per share	\$ (2.11)	\$ (1.71)
	=====	=====
EBITDA	(48,636)	(18,431)
	=====	=====

Z-Tel Technologies, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(In thousands, except share data)

	September 30, 2000	December 31, 1999
	----- (Unaudited)	-----
Assets		
Current assets:		
Cash and cash equivalents	\$ 23,383	\$ 101,657
Accounts receivable	52,719	4,245
Prepaid expenses and other current assets	5,088	2,304
	-----	-----
Total current assets	81,190	108,206
Property and equipment, net	55,014	28,549
Investments	5,704	--
Intangible assets, net	64,738	--
Other	3,388	922
	-----	-----
Total assets	\$ 210,034	\$ 137,677
	=====	=====
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 31,803	\$ 9,165
Current portion of long-term debt and capital lease obligations	7,617	3,726
	-----	-----
Total current liabilities	39,420	12,891
Long-term debt and capital lease obligations	13,923	10,408
	-----	-----
Total liabilities	53,343	23,299
	-----	-----
Mandatorily convertible redeemable preferred stock	40,657	
Mandatorily redeemable common stock warrants	16,475	

Stockholders' equity:		
Common stock	339	322
Notes receivable from stockholders	(789)	(1,683)
Unearned stock compensation	(121)	(2,487)
Additional paid-in capital	205,528	167,637
Accumulated deficit	(109,733)	(49,093)
Accumulated other comprehensive income	4,653	--
Treasury stock	(318)	(318)
	-----	-----
Total stockholders' equity	99,559	114,378
	-----	-----
Total liabilities and stockholders' equity	\$ 210,034	\$ 137,677
	=====	=====

CONTACT: Z-Tel Technologies Inc., Tampa
Mark H. Johnson, 813/233-4610
mjohnson@z-tel.com

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SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

(MARK ONE)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF
THE SECURITIES EXCHANGE ACT OF 1934
FOR THE YEAR ENDED DECEMBER 31, 1999

OR

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

For the transition period from _____ TO _____

COMMISSION FILE NUMBER: 000-28467

Z-TEL TECHNOLOGIES, INC.

(Exact name of Registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

59-3501119
(I.R.S. Employer
Identification Number)

601 South Harbour Island Boulevard, Suite 220
Tampa, Florida 33602
(813) 273-6261

(Address, including zip code, and telephone number
including area code, of Registrant's principal executive offices)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: Common Stock, par value
\$.01 per share

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10 K.

The aggregate market value of the Registrant's Common Stock held by non-affiliates of the Registrant on March 23, 2000 (assuming solely for these purposes that all directors, executive officers and 10% or greater stockholders are affiliates), based on the closing price of the Common Stock on the Nasdaq National Market as of such date, was approximately \$777,720,354.

The number of shares of the Registrant's Common Stock outstanding as of March 23, 2000 was approximately 32,006,661.

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PART I

ITEM 1. BUSINESS

GENERAL

Z-Tel Technologies, Inc. was incorporated under the laws of Delaware in 1998. We are a provider of advanced, integrated communications services primarily to residential customers. We offer local and long distance telephone services in combination with enhanced communications features accessible through the telephone or the Internet. Through our uniquely designed web interface, our subscribers are able to manage their communications through the power of the Internet and the visual, "point and click" functionality of the personal computer. Our services are designed to make communications easier and more efficient.

Our business strategy takes advantage of recent statutory and regulatory changes that enable us to gain access to the individual components of the traditional local telephone service provider's (incumbent local exchange carrier or ILEC) networks, referred to as the unbundled network element platform. The Federal Communications Commission (the FCC) has recently mandated that the incumbent local exchange carriers provide competing local telephone companies such as us with the unbundled network element platform components at prices based on a forward-looking, long-run incremental cost methodology. Access to these components, in combination with our proprietary technology and advanced communications network, enables us to provide cost-effective local and long distance telephone services with enhanced features.

We currently offer our Z-Line Home Edition(TM) service in areas of New York and, on an initial marketing basis, in areas of Massachusetts served by Bell Atlantic Corporation (Bell Atlantic), and in areas of Texas served by Southwestern Bell Telephone Company (Southwestern Bell). Within these markets, we believe that we are one of few competitive local exchange carriers specifically targeting the needs of residential customers. It is our intent to expand service into additional areas as they become available. In particular, we intend to begin initial marketing of Z-Line Home Edition in Pennsylvania in the second quarter of 2000.

We currently offer three services to individual customers, Z-Line Home Edition, Z-Line Anywhere(TM) and Z-Line Messenger(TM), each centered around Your Personal Communications Center(TM) (the PCC). The PCC includes multiple features that combine the convenience of the telephone with the power of the Internet. Accessible by telephone or the Internet, located at www.myzline.com or www.z-tel.com, the PCC enables our customers to direct, retrieve, deliver, compile and otherwise manage their voice communications. One of the features offered through the PCC is the Z-Line Community(TM) feature, which allows us to provide group messaging features to individual consumers as well as sponsored communities such as colleges, civic organizations and businesses. We intend to begin offering soon an additional service to individual customers, Z-Line Long Distance(TM).

ACQUISITION OF TOUCH 1 COMMUNICATIONS, INC.

On January 24, 2000, we reached an agreement in principle with Touch 1 Communications, Inc. (Touch 1) for the acquisition of Touch 1, a transaction which will bring together our bundled

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consumer telecommunications services with Touch 1's extensive telemarketing, customer service and provisioning infrastructure. Touch 1 is a leading consumer telecommunications company with approximately 400,000 customers in 48 states. Touch 1 produced revenues for 1999 of approximately \$65 million. The transaction, which is subject to, among other things, the signing of a definitive agreement, other regulatory approvals, and customary closing conditions, is expected to close before the end of May 2000.

INDUSTRY BACKGROUND

The Telecommunications Act of 1996 (the Telecommunications Act) was passed principally to foster competition in the telecommunications markets. The Telecommunications Act imposes a variety of duties upon the incumbent local exchange carriers, including the duty to provide other communications companies with access to their network elements on an unbundled basis at any feasible point. Such access must be at rates and on terms and conditions that are just, reasonable and nondiscriminatory. A network element is a facility or piece of equipment of the local telephone company's network or the features, functions or capabilities such facility or equipment provides. The Telecommunications Act also establishes procedures under which the Regional Bell Operating Companies (Bell operating companies) will be allowed to handle long distance calls originating from within their telephone service area and terminating outside their area. The Bell operating companies were divested by AT&T in 1984 pursuant to court order under which they were prohibited from providing "in-region" long distance telephone service. With the passage of the Telecommunications Act, a Bell operating company can provide such in-region service if it complies with a 14-point regulatory checklist, including offering interconnection to other communications companies and providing access to its unbundled network elements on terms approved by a state public service commission.

On September 10, 1999, in an effort to comply with the 14-point regulatory checklist in order to be able to offer "in-region" long distance telephone service, Bell Atlantic filed a tariff which establishes favorable rates, terms and conditions under which competitors may purchase unbundled network elements in New York. In its New York tariff, Bell Atlantic committed to provide unbundled network elements, both individually and on a combined basis, for provision of residential telephone service and small business telephone service, with the exclusion of business service from end offices with two or more competitive local telephone service providers (CLECs) collocated in that end office.

On November 5, 1999, the FCC released an order establishing the list of unbundled network elements that incumbent local exchange carriers nationwide must provide. Taken together, these unbundled network elements comprise the most important facilities, features, functions and capabilities of an incumbent local exchange carrier's network. Under the FCC's order, the incumbent local exchange carriers must allow competing local telephone companies such as us to use the unbundled network elements, in an individual or combined fashion, to provide basic local telephone service and must price the elements using a forward-looking, long-run incremental cost methodology. We expect both individual network components and components in combined component service packages to be available at attractive prices nationwide as state regulatory authorities and incumbent local exchange carriers conform to the recent FCC mandates. Pricing and implementation rules for unbundled network elements in

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combined service packages or platform offerings that are at least acceptable for market entry have been adopted in New York, Pennsylvania, Texas and Massachusetts. The prices for the use of individual network components and combined component service packages will nevertheless vary from state to state, as will an individual state's oversight of unbundled network element platform implementation and operation.

BUSINESS OVERVIEW

By integrating the simplicity of standard telephone service with the robust features that our Internet applications deliver, we have created an environment for managing communications that is accessible by the telephone or personal computer. That environment includes the following elements:

COST-EFFECTIVE BUNDLED LOCAL AND LONG DISTANCE TELEPHONE SERVICE. We provide a cost-effective bundled package of local and long distance telephone services, which includes all the enhanced features of the PCC as well as enhanced telephone services such as call waiting and caller identification, in markets that have favorable regulatory environments to residential customers in those markets. We lease facilities of the existing incumbent local exchange carrier at a forward-looking, long-term incremental cost basis, which enables us to avoid the need to invest significant capital into switching equipment at the incumbent local exchange carrier's central office. As a result, we are able to provide a competitively priced, bundled package that includes local and long distance telephone services and enhanced services.

SEAMLESS INTEGRATION OF PERSONAL ORGANIZATIONAL TOOLS. The PCC has been designed to allow users to download their personal directories from a variety of software packages, including Microsoft Outlook. In addition, other personal contact managers, such as Palm Pilot, can be downloaded into Outlook and then downloaded into the PCC. Once this information has been downloaded, customers can use their database of contacts to create easily sub-directories for special group messaging. By utilizing the PCC, customers can, with the click of a mouse, initiate calls or forward messages to contacts that have been stored in their personal directories. We believe the ability to manage personal directories on our network creates a more loyal customer over time because of the difficulty of transferring personal directories to other services.

SCALABLE PLATFORM FOR NEW MARKETS. The unbundling of network elements allows us to access the incumbent local exchange carriers' facilities to provision our service to our customers. As a result, we have the ability to enter new markets quickly, and without a significant investment in equipment, as regulatory authorities in those markets adopt favorable pricing. In addition, we have a centralized sales staff that receives incoming calls for new service and electronically provides service to new customers. Using the PCC, customers can manage and configure their own service requirements, thus minimizing our need for an expanded customer service infrastructure.

ADVANCED PROPRIETARY TECHNOLOGY. We have created an integrated and proprietary software and advanced network architecture that enables the enhanced features of our service. We have created software applications that can control the basic functions of initiating and completing a telephone call regardless of the access device, such as a telephone or personal

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computer. These applications allow our customers to control simultaneously all the basic functions of a telephone call from either the telephone or personal computer. In addition, we, in collaboration with a third party, have created our own proprietary billing system. We are also in the process of developing and enhancing our customer care, billing and provisioning software into one seamlessly integrated package.

Our network is designed to route traffic to our main enterprise management center in Tampa for call management. This reduces our need to collocate network equipment in the central offices of the incumbent local exchange carrier in our target markets and enhances our ability to enter new markets quickly and cost effectively. Our network architecture also is designed to accommodate a number of developing technologies, such as telephone calls over Internet protocol, digital subscriber line, asynchronous transfer mode, or coaxial cable systems.

ENHANCED COMMUNICATION SERVICES FOR GROUPS AND INDIVIDUAL USERS NATIONWIDE. We offer our Z-Line Community features to consumers, organizations and business users nationwide through the PCC. Those features may be accessed from any of our services. The PCC capabilities, including specialized features for directories and group messaging, provide value to users within sponsored communities by facilitating communication among dispersed community members.

We intend to pursue Z-Line Home Edition marketing and distribution in new states as state regulatory authorities impose favorable pricing, implementation rules and acceptable operations support systems performance for the unbundled network element platform components. Favorable implementation requirements for providing the unbundled network element platform components were a feature of the SBC Communications, Inc./Ameritech Corporation merger order conditions recently approved by the FCC. Accordingly, as acceptable pricing and operations support systems become available, we intend to evaluate the entry into each state in the combined SBC/Ameritech regions. Similar requirements are currently being discussed by the FCC with regard to conditions likely to be required in association with the approval of the pending Bell Atlantic/GTE merger. Furthermore, U S WEST Corporation and BellSouth Corporation recently announced the general availability of the unbundled network element platform components as part of a general effort to meet FCC requirements.

SERVICES

Z-LINE HOME EDITION

Z-Line Home Edition is our principal service offering and is currently being offered in New York, Texas and, on an initial marketing basis, in Massachusetts, in areas serviced by the Bell operating company operating in those states. Z-Line Home Edition includes low-priced local and long distance (1+) residential telephone services using a customer's existing telephone number, bundled with enhanced features, including caller identification, call forwarding, three-way calling, call waiting and speed calling, dial-up remote access through our Z-Line Anywhere access card service, the full functionality of the PCC and, for an additional fee, Internet access.

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We intend to pursue offering Z-Line Home Edition in additional states as soon as favorable pricing and implementation rules are imposed in those states, and to start marketing Z-Line Home Edition in Pennsylvania before the end of the second quarter of 2000.

Z-LINE ANYWHERE

Z-Line Anywhere is our access card service that allows a customer to make long-distance calls using Z-Tel's network from any phone simply by dialing a toll-free 800 number or local access number. No change in phone service is required. Customers of Z-Line Anywhere also receive the full functionality of the PCC and, for an additional fee, Internet access. Z-Line Anywhere is being offered nationwide.

Z-LINE MESSENGER

Z-Line Messenger is a trial service we offer to consumers and members of sponsored communities free of charge that provides certain limited features of the PCC. Z-Line Messenger customers are limited to sixty minutes of voice mail per month and are not authorized to use certain enhanced services provided by the PCC, such as the ability to complete a call using the web, the "Find-Me" functionality and the ability to create and manage "Communities." Customers may upgrade their service to Z-Line Anywhere or Z-Line Home Edition, provided that that latter service is offered in their markets. Z-Line Messenger is being offered nationwide.

Z-LINE LONG DISTANCE

Z-Line Long Distance is a usage-based service currently in development that will allow customers to use us as their primary long-distance calling provider to complete their residential long distance (1+) calls. Z-Line Long Distance will also provide our customers with dial-up remote access through our Z-Line Anywhere access card product, the full functionality of the PCC and, for an additional fee, Internet access. We intend to offer Z-Line Long Distance nationwide in the near future.

KEY FEATURES OF OUR SERVICES

THE PCC

The PCC is the core feature set of all of our service offerings, although only limited functionality is provided to Z-Line Messenger customers. It is a suite of features subscribers can access via any telephone or at our web site. Subscribers can retrieve, forward, deliver, store, compile and otherwise manage their voice mail and other communication needs. Using the "Find-Me" feature, subscribers can have the PCC attempt to locate them at up to three numbers when they receive incoming calls, and notify them via e-mail, pager or ICQ Internet Chat (instant messaging) when a new voice mail message arrives. At our website, subscribers can view a list of their voice mail messages and listen to them through their computer speakers, create an on-line Address Book by inputting information directly or importing it from other services, place calls with the click of a mouse, deliver voice messages to groups of other subscribers, forward voicemails and view historical billing statements on-line.

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We expect to provide additional functionality to the PCC in the future, including the ability to use the PCC in conjunction with personal digital assistants (PDAs), voice recognition capability, the ability to use the PCC for conference calling, the ability to manipulate voicemail and Z-Line settings from the user's desktop, and dedicated e-mail accounts and fax receiving capability.

Z-LINE COMMUNITY

Z-Line Community is a set of features embedded within the PCC that allows users or group sponsors to search for, create or join "Communities," which are pre-defined groups of our users usually based on professional or personal affinities. Users can also invite other of our subscribers to join Communities and administrate the user access options of a Community. Once the Communities are created, users can send group messages to specific members of the communities or the entire group.

Z-Line Community enables us to offer sponsored communities such as colleges, civic organizations and businesses with a robust communication solution. Each community member automatically receives our Z-Line Messenger trial product and can thereby gain access to limited features of the PCC, including Z-Line Community, and can upgrade to any of our other service offerings. Community members can then interact with one another, even when the individual community members have subscribed to different services.

Z-Line Community features benefit both the sponsor and members of a community. Sponsors can use group messaging features to deliver voice mail messages to their widely-dispersed members. Colleges, for instance, can use our services to deliver simultaneously voice mail messages, including personalized information such as financial aid and class schedule updates, to their widely dispersed students. Students, faculty and administrators can take advantage of low long distance rates by upgrading their Z-Line Messenger service, or set up their own sub-communities based on student groups or other affiliations, and can use our network to disseminate information to community members.

MARKETING AND DISTRIBUTION

We market our services to our customers through telemarketing, agent programs, strategic business partnerships, direct mail and marketing and traditional advertising campaigns promoting recognition and awareness of our "Z" brand. We also have entered into joint marketing or co-branding arrangements with organizations that have large, well-established relationships or customer bases in our target markets, such as Hofstra University, the Fraternal Order of Police, the Fire Fighters' Association of Texas and Kinkos.com. We intend to explore the formation of alliances or ventures with other companies, including Internet service providers, paging operators, cable television companies, utilities, newspapers, banks, credit card companies and department stores, which we believe will allow us to penetrate efficiently large customer bases with a relatively small capital outlay.

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BILLING AND COLLECTION

We have three primary methods for billing and collecting from our customers. For our Z-Line Home Edition customers, we can either (1) charge their credit card account; (2) mail a bill to their address for payment by check; or (3) set up an automatic withdrawal from the customer's checking account. For our Z-Line Anywhere customers, we currently require all new customers to pay by credit card or automatic withdrawal; however, we had, in the past, allowed them to pay bills using all three methods. Our billing software can be customized to handle new and different billing programs.

OPERATIONS SUPPORT SYSTEMS AND CUSTOMER SUPPORT

We have invested substantially in our software platform, which includes integrated customer ordering and provisioning, customer service and billing functionality for our services. For our Z-Line Anywhere service, a new subscriber can enroll via the Internet or our toll free number with service immediately activated. The PCC allows our Z-Line Home Edition and Z-Line Anywhere customers to change billing options and service feature configurations. A subscriber may also update service configurations on the telephone.

Z-Line Home Edition orders require us to interact with the applicable local exchange carrier. Currently, after receiving a signed letter of authorization or a verified verbal request for service, we enter orders using an electronic web-based interface provided by Bell Atlantic for our New York and Massachusetts customers and Southwestern Bell for our Texas customers. Our provisioning agents also enter the order in the Z-Tel system.

We expect to invest over the next year to expand our operations support systems to include electronic gateways to the major incumbent local exchange carriers, network element management software, and a standard internal provisioning interface that can handle multiple incumbent local exchange carrier ordering systems. This investment will include outside integration and consulting assistance.

INTELLECTUAL PROPERTY AND PROPRIETARY RIGHTS

We have developed proprietary software that manages the integrated features of our service offerings. Our software allows our network to interface and interconnect with the systems of the incumbent local exchange carriers and long-distance carriers. In addition, our software allows our remote network communication facilities, which we call "Z-Nodes," located throughout the United States, to communicate with each other and with our enterprise management center in Tampa, Florida.

Our intellectual property reflects the know-how, work product and inventions of over eighty engineers in our research and development team, based at our technology center in Atlanta, Georgia, who have substantial experience in computer technology, telecommunications, web-based services, database management and integration, and network development, architecture, operation and management.

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For the fiscal years ended December 31, 1999 and 1998, we invested approximately \$8,356,000 and \$4,728,000, respectively, in company-sponsored research and development activities.

We have entered into, and will continue to enter into, nondisclosure agreements with our employees, independent contractors, business customers and others. We believe these agreements will protect our confidential and proprietary information, whether or not such information is copyrighted or subject to trademark or patent protection. We intend to take all appropriate legal action to protect our ownership and the confidentiality of all our proprietary software, including, as appropriate, the filing of copyrights in the U.S. Copyright Office.

We have filed trademark applications for federal registration of more than fifty trademarks with the United States Patent and Trademark Office including Z-TEL, Z-TEL TECHNOLOGIES, INC., Z-TEL COMMUNICATIONS, INC. AND DESIGN, Z-LINE HOME EDITION, Z-LINE ANYWHERE, Z-NODE, Z-LINE, Z-NOTIFY, Z-SITE, Z-MAILBOX, Z-DIRECTORY, Z-NOW!, Z-NUMBER, Z-BILL PAYMENT SERVICES, Z-NET, GENERATION Z, MYZLINE, YOUR PERSONAL TELECOMMUNICATIONS PORTAL and YOUR PERSONAL COMMUNICATIONS CENTER.

COMPETITION

OVERVIEW

The telecommunications industry is highly competitive in many market segments. However, at present, we believe few telecommunications carriers provide the type of bundled packages that include the range of services and features we offer, but various competitors offer one or more of the services that make up our service offering. Competition in the local telephone services market is still emerging, but already has attracted many strong competitors. Competition in the long distance and information services markets, which have fewer entry barriers, is already intense and is expected to remain so.

We believe the principal competitive factors affecting our business will be the quality and reliability of our services, innovation, customer service and price. Our ability to compete effectively will depend upon our continued ability to offer innovative, high-quality, market-driven services at prices generally equal to or below those charged by our competitors. Many of our current and potential competitors have greater financial, marketing, personnel and other resources than we do, as well as other competitive advantages.

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LOCAL TELEPHONE SERVICE

INCUMBENT LOCAL EXCHANGE CARRIERS. In each of our target markets, we will compete with the incumbent local exchange carrier serving that area, which may be one of the Bell operating companies. As a recent entrant in the telecommunications services industry, we have not achieved and do not expect to achieve a significant market share for any of our services in our markets in the foreseeable future. In particular, the incumbent local exchange carriers have long-standing relationships with their customers, have financial, technical and marketing resources substantially greater than ours, have the potential to subsidize services that compete with our services with revenue from a variety of other unregulated businesses, and currently benefit from certain existing regulations that favor the incumbent local exchange carriers over us in certain respects.

Recent regulatory initiatives that allow competitive local exchange carriers, such as us, to interconnect with incumbent local exchange carrier facilities and acquire and combine the unbundled network elements of an incumbent local exchange carrier provide increased business opportunities for us. However, such interconnection opportunities have been, and likely will continue to be, accompanied by increased pricing flexibility and relaxation of regulatory oversight for the incumbent local exchange carriers.

COMPETITIVE LOCAL EXCHANGE CARRIERS. The Telecommunications Act radically altered the market opportunity for competitive local exchange carriers. Competitive access providers who entered the market prior to passage of the Telecommunications Act built their own infrastructure to offer exchange access services to large end-users. Since the passage of the Telecommunications Act, many competitive access providers have added switches to become competitive local exchange carriers in order to take advantage of the opening of the local market. With the Telecommunications Act requiring unbundling of the incumbent local exchange carrier's networks, competitive local exchange carriers will now be able to enter the market more rapidly by leasing switches, trunks and loop capacity until traffic volume justifies building facilities. Newer competitive local exchange carriers, like us, will not have to replicate existing facilities and can be more opportunistic in designing and implementing networks, which could have the effect of increasing competition for local exchange services.

INTEREXCHANGE CARRIERS. We also expect to face competition from other current and potential market entrants, including interexchange (long distance) carriers such as AT&T, MCI WorldCom, and Sprint, seeking to enter, reenter or expand entry into the local exchange market. A continuing trend toward consolidation of telecommunications companies and the formation of strategic alliances within the telecommunications industry, as well as the development of new technologies, could give rise to significant new competitors. For example, in September 1998, WorldCom merged with MCI Communications Corp. and, in October 1999, MCI WorldCom and Sprint Communications Company, L.P. announced merger plans. In March 1999, AT&T acquired Tele-Communications, Inc., the largest provider of cable television services in the United States. These types of consolidations and strategic alliances could put us at a competitive disadvantage.

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LONG DISTANCE TELEPHONE SERVICE

The long distance telecommunications industry has numerous entities competing for the same customers and a high average churn rate because customers frequently change long distance providers in response to the offering of lower rates or promotional incentives by competitors. Our primary competitors in the long distance market include major interexchange carriers such as AT&T, MCI WorldCom, Sprint and Qwest Communications International Inc., certain incumbent local exchange carriers and resellers of long distance services. We believe that pricing levels are a principal competitive factor in providing long distance telephone service. We hope to avoid direct price competition by bundling long distance telephone service with a wide array of value-added services.

Incumbent local exchange carriers that offer a package of local, long distance telephone and information services will be particularly strong competitors. Incumbent local exchange carriers, including Bell Atlantic, are currently providing both long distance and local services as well as certain enhanced telephone services we offer. We believe that the Bell operating companies will attempt to offset market share losses in their local markets by attempting to capture a significant percentage of the long distance market.

ENHANCED SERVICES

We compete with a variety of enhanced service companies. Enhanced services markets are highly competitive, and we expect that competition will continue to intensify. Our competitors in these markets will include Internet service providers, web-based communications service providers and other telecommunications companies, including the major interexchange carriers, incumbent local exchange carriers, competitive local exchange carriers and wireless carriers.

OTHER MARKET ENTRANTS

We may face competition in local, long distance and information services from other market entrants such as electric utilities, cable television companies, fixed and mobile wireless system operators, and operators of private networks built for large end-users. All of these companies are free to offer bundled services similar to those that we offer. Electric utilities have existing assets and low cost access to capital that could allow them to enter a market rapidly and accelerate network development. Cable television companies are also entering the telecommunications market by upgrading their networks with fiber optics and installing facilities to provide fully interactive transmission of broadband voice, video and data communications. Wireless companies have developed, and are deploying in the United States, wireless technology as a substitute for traditional wireline local telephones. The recent World Trade Organization agreement on basic telecommunications services could increase the level of competition we face. Under this agreement, the United States and 68 other member states of the World Trade Organization committed to open their respective telecommunications markets, including permitting foreign companies to enter into basic telecommunications services markets. This development may increase the number of established foreign-based telecommunications carriers entering the U.S. markets.

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The Telecommunications Act includes provisions that impose certain regulatory requirements on all local exchange carriers, including competitive local exchange carriers. At the same time, the Telecommunications Act expands the FCC's authority to reduce the level of regulation applicable to any or all telecommunications carriers, including incumbent local exchange carriers. The manner in which these provisions are implemented and enforced could have a material adverse effect on our ability to compete successfully against incumbent local exchange carriers and other telecommunications service providers.

GOVERNMENT REGULATION

OVERVIEW

Some of our services are regulated and some are not. In providing our non-common carrier services such as voice mail, "Find-Me," notification and directory services offered through the PCC, we operate as an unregulated provider of information services, as that term is defined in the Communications Act of 1934, as amended by the Telecommunications Act of 1996, and as an enhanced service provider, as that term is defined in the FCC rules. These operations currently are not regulated by the FCC or the states where we operate. In providing Z-Line Home Edition and our long distance services, we are regulated as a common carrier at the state and federal level and are subject to additional rules and policies not applicable to providers of information services alone. We are certificated as a facilities-based competitive local exchange carrier in a number of states, including New York, Texas, Massachusetts, Pennsylvania, Georgia, Illinois, New Jersey, Florida, Kentucky, Missouri, Oregon, Virginia and Washington. We are currently seeking this certification in additional states, including California and Michigan.

The local and long distance telecommunications services we provide are regulated by federal, state, and, to some extent, local government authorities. The FCC has jurisdiction over all telecommunications common carriers to the extent they provide interstate or international communications services. Each state regulatory commission has jurisdiction over the same carriers with respect to the provision of intrastate communications services within that state. Local governments sometimes seek to impose franchise requirements on telecommunications carriers and regulate construction activities involving public rights-of-way. Changes to the regulations imposed by any of these regulators could have a material adverse effect on our business, operating results and financial condition.

In recent years, the regulation of the telecommunications industry has been in a state of flux as the United States Congress and various state legislatures have passed laws seeking to foster greater competition in telecommunications markets. The FCC and state utility commissions have adopted many new rules to implement this legislation and encourage competition. These changes, which are still incomplete, have created new opportunities and challenges for us and our competitors. The following summary of regulatory developments and legislation is intended to describe the most important, but not all, present and proposed federal, state and local regulations and legislation affecting the telecommunications industry. Some of these and other existing federal and state regulations are the subject of judicial proceedings and legislative and administrative proposals which could change, in varying degrees, the manner in

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which this industry operates. We cannot predict the outcome of any of these proceedings or their impact on the telecommunications industry at this time. Some of these future legislative, regulatory or judicial changes may have a material adverse impact on our business.

Specifically, as states re-evaluate pricing of network elements, it is possible that some states could increase rates over existing levels. Currently, Bell Atlantic and Southwestern Bell have rate cases pending before state regulatory commissions in New York and Illinois that could significantly raise the existing rates for some network elements and network element combinations. Our intent is to be an active participant in these rate cases and any others that might be critical to our operations. We anticipate joining other competitive service providers in arguing that existing rates are overstated and do not reflect the true total element long run incremental costing principles required by the FCC and the Telecommunications Act. While the prevailing trends within the industry would predict the adoption of lower rates in association with the provision of unbundled network elements and network element combinations, we cannot predict the outcome of any pending or potential rate case. Increases or decreases in rate levels charged by incumbent local exchange carriers as a result of regulatory review through rate case or arbitration proceedings could significantly impact our business plans.

FEDERAL REGULATION

FCC POLICY ON ENHANCED AND INFORMATION SERVICES

In 1980, the FCC created a distinction between basic telecommunications services, which it regulates as common carrier services, and enhanced services, which remain unregulated. The FCC exempted enhanced service providers from federal regulations governing common carriers, including the obligation to pay access charges for the origination or termination of calls on carrier networks and the obligation to contribute to universal service. The Telecommunications Act of 1996 established a similar distinction between telecommunications services and information services. Changing technology and changing market conditions, however, sometimes make it difficult to discern the boundary between unregulated and regulated services.

In general, information services are value-added services that use regulated transmission facilities only as part of a services package that also includes network or computer software to change or enhance the information transmitted. We believe that most of the services we provide, including voice mail, "Find-Me" notification, and directory services offered through the PCC are information services under the FCC's definition. Because the regulatory boundaries in this area are somewhat unclear and subject to dispute, however, the FCC could seek to characterize some of our information services as "telecommunications services." If that happens, those services would become subject to FCC regulation, although the impact of that reclassification is difficult to predict.

In general, the FCC does not regulate the rates, services, and market entry and exit of non-dominant telecommunications carriers, but does require them to contribute to universal service and comply with other regulatory requirements. We are currently regulated as non-dominant with respect to both our local and long distance telephone services.

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FCC REGULATION OF COMMON CARRIER SERVICES

We currently are not subject to price cap or rate of return regulation at the federal level and are not currently required to obtain FCC authorization for the installation, acquisition or operation of our domestic exchange or interexchange network facilities. However, we must comply with the requirements of common carriage under the Communications Act of 1934. We are subject to the general requirement that our charges and terms for our telecommunications services be "just and reasonable" and that we not make any "unjust or unreasonable discrimination" in our charges or terms. The FCC has jurisdiction to act upon complaints against any common carrier for failure to comply with its statutory obligations.

Comprehensive amendments to the Communications Act of 1934 were made by the Telecommunications Act of 1996, which was signed into law on February 8, 1996. The Telecommunications Act effected changes in regulation at both the federal and state levels that affect virtually every segment of the telecommunications industry. The stated purpose of the Telecommunications Act is to promote competition in all areas of telecommunications. While it may take years for the industry to feel the full impact of the Telecommunications Act, it is already clear that the legislation provides us with new opportunities and challenges.

INTERCONNECTION. The Telecommunications Act greatly expands the interconnection requirements applicable to the incumbent local exchange carriers, i.e., generally, those existing local exchange carriers that, in the past, enjoyed virtual or legal monopoly status. The Telecommunications Act requires the incumbent local exchange carriers to

- o provide physical collocation, which allows companies such as us and other competitive local exchange carriers to install and maintain our own network termination equipment in incumbent local exchange carrier central offices or, if requested or if physical collocation is demonstrated to be technically infeasible, virtual collocation;
- o offer components of their local service networks on an unbundled basis so that other providers of local service can use these elements in their networks to provide a wide range of local services to customers; and
- o establish "wholesale" rates for their services to promote resale by competitive local exchange carriers. We currently do not have plans to enter any markets by reselling incumbent local exchange carrier service.

In addition, all local exchange carriers must

- o interconnect with the facilities of other carriers;
- o establish number portability, which will allow customers to retain their existing phone numbers if they switch from the local exchange carrier to a competitive local service provider;

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- o provide nondiscriminatory access to telephone poles, ducts, conduits and rights-of-way; and
- o compensate other local exchange carriers on a reciprocal basis for traffic originated by one local exchange carrier and terminated by another local exchange carrier.

The FCC is charged with establishing national guidelines to implement certain portions of the Telecommunications Act. The FCC issued its interconnection order on August 8, 1996. Among other rules, the FCC established a list of seven network elements, comprising most of the significant facilities, features, functionalities, or capabilities of the network, that the incumbent local exchange carriers must unbundle. It is possible for competitors to provide competitive local exchange service using only these unbundled network elements. In addition, the FCC mandated a particular forward looking pricing methodology for these network elements that produces relatively low element prices that are favorable to competitors.

On July 18, 1997, however, the United States Court of Appeals for the Eighth Circuit issued a decision vacating the FCC's pricing rules, as well as certain other portions of the FCC's interconnection rules, on the grounds that the FCC had improperly intruded into matters reserved for state jurisdiction. On January 25, 1999, the Supreme Court largely reversed the Eighth Circuit's order, holding that the FCC has general jurisdiction to implement the local competition provisions of the Telecommunications Act. In so doing, the Supreme Court stated that the FCC has authority to set pricing guidelines for unbundled network elements, to prevent incumbent local exchange carriers from disaggregating existing combinations of network elements, and to establish "pick and choose" rules regarding interconnection agreements. "Pick and choose" rules would permit a carrier seeking interconnection to pick and choose among the terms of service from other interconnection agreements between the incumbent local exchange carriers and other competitive local exchange carriers. This action reestablishes the validity of many of the FCC rules vacated by the Eighth Circuit.

Although the Supreme Court affirmed the FCC's authority to develop pricing guidelines, the Supreme Court did not evaluate the specific forward-looking pricing methodology mandated by the FCC and has remanded the case to the Eighth Circuit for further consideration. Some incumbent local exchange carriers have argued that this pricing methodology does not allow adequate compensation for the provision of unbundled network elements. The Eighth Circuit heard oral arguments on this pricing issue on September 16, 1999, but has not yet issued a ruling.

The Supreme Court also remanded the list of unbundled network elements to the FCC for further consideration of the necessity of each one under the statutory standard. On November 5, 1999, the FCC released an order largely retaining its list of unbundled network elements, but eliminating the requirement that incumbent local exchange carriers provide unbundled access to local switching for customers with four or more lines in the densest parts of the top 50 Metropolitan Statistical Areas, and to operator services and directory assistance. The FCC concluded that the market has developed since 1996 such that competitors can and do self-provision these services, or acquire them from alternative sources. The FCC also noted that incumbent local exchange carriers remain obligated under the non-discrimination requirements of the Communications Act of 1934 to comply with the reasonable request of a carrier that

purchases these services from the incumbent local exchange carriers to rebrand or unbrand those services, and to provide directory assistance listings and updates in daily electronic batch files. In addition, the competitive checklist contained in Section 271 of the Communications Act of 1934 requires Bell operating companies to provide nondiscriminatory access to these services.

These new FCC rules are likely to be the subject of further appeals. Thus, while the Supreme Court resolved many issues, including the FCC's jurisdictional authority, other issues remain subject to further consideration by the courts and the FCC. We cannot predict the ultimate disposition of those matters. If the Eighth Circuit fails to affirm the FCC's pricing methodology--which is favorable to competitors such as us because it is based on forward-looking costs--then unbundled network element prices, including prices for unbundled network element combinations, may rise. Such increases could have a materially adverse effect on our business.

INTERCONNECTION AGREEMENTS. The Telecommunications Act obligates incumbent local exchange carriers to negotiate with us in good faith to enter into interconnection agreements. Competitive local exchange carriers like us can purchase unbundled network elements under such an agreement or under a tariff or a Statement of Generally Available Terms filed with the state regulators. Although we purchase the unbundled network element platform in New York under Bell Atlantic's tariff, we will need interconnection agreements in some states, and have entered into interconnection agreements in Texas, Massachusetts and Pennsylvania, to provide enhanced connectivity to our network and to provide local exchange services, including Z-Line Home Edition. If we cannot reach agreement, either side may petition the applicable state commission to arbitrate remaining disagreements. These arbitration proceedings can last for a substantial period of time. Moreover, state commission approval of any interconnection agreement resulting from negotiation or arbitration is required, and any party may appeal an adverse decision by the state commission to federal district court, although some federal district courts have refused to exercise jurisdiction over such cases. The potential cost in resources and delay from this process could harm our ability to compete in certain markets, and there is no guarantee that a state commission would resolve disputes, including pricing disputes, in our favor.

COLLOCATION AND LINE SHARING. The FCC recently adopted new rules designed to make it easier and less expensive for competitive local exchange carriers to obtain collocation at incumbent local exchange carriers' central offices by, among other things, restricting the incumbent local exchange carriers' ability to prevent certain types of equipment from being collocated and requiring incumbent local exchange carriers to offer alternative collocation arrangements. On November 18, 1999, the FCC also adopted a new order requiring incumbent local exchange carriers to provide line sharing, which will allow competitive local exchange carriers to offer data services over the same line that a consumer uses for voice services without the competitive local exchange carriers' having to provide the voice service. While we expect that the FCC's new rules will be beneficial to competitive local exchange carriers, we cannot be certain that these new rules will be implemented by the incumbent local exchange carrier in a timely or favorable manner. Moreover, incumbent local exchange carriers and other parties have asked the FCC to reconsider portions of these rules. In addition, on March 17, 2000, the United States Court of Appeals for the District of Columbia Circuit vacated portions of the FCC's new collocation rules. Specifically, the court found that the FCC's interpretation of the statutory terms "necessary" and "physical collocation" are impermissibly broad, and remanded those portions of the order to the FCC for reconsideration. We cannot predict the outcome of these actions or the effect they may have on our business.

BELL OPERATING COMPANY ENTRY INTO THE LONG DISTANCE MARKET. The Telecommunications Act permitted the Bell operating companies to provide long distance services outside their local service regions immediately, and will permit them to provide in-region long distance service upon demonstrating to the FCC and state regulatory agencies that they have adhered to the Telecommunication Act's Section 271 14-point competitive checklist. Some Bell operating companies have filed applications with various state public utility commissions and the FCC seeking approval to offer in-region interLATA service. Some states have denied these applications while others have approved them. Prior to December 1999, the FCC had denied each of the Bell operating company applications brought before it because it found that the particular Bell operating company had not sufficiently made its local network available to competitors. On September 29, 1999, Bell Atlantic filed with the FCC an application to provide in-region long distance service originating in New York. The FCC issued an order allowing Bell Atlantic to enter the in-region long distance market in New York in late-December 1999. Bell Atlantic began offering long distance service in New York on a commercial basis in January 2000. On January 10, 2000, Southwestern Bell filed an application with the FCC seeking approval to offer in-region interLATA services in Texas. By statute, the FCC must act on that application by April 10, 2000. While we cannot predict the outcome of any Section 271 applications before the FCC, it is generally expected that long distance competition will increase as the Bell operating companies enter the market. We also expect other Bell operating companies to file similar applications in 2000 and 2001.

UNIVERSAL SERVICE. In May 1997, the FCC released an order establishing a significantly expanded universal service regime to subsidize the cost of telecommunications service to high cost areas, as well as to low-income customers and qualifying schools, libraries and rural health care providers. Providers of interstate telecommunications services, like us, as well as certain other entities, must pay for these programs. We are also eligible to receive funding from these programs if we meet certain requirements, but we do not currently have plans to do so. Our share of the payments into these subsidy funds will be based on our share of certain defined telecommunications end-user revenues. Currently, the FCC is assessing such payments on the basis of a provider's revenue for the previous year. Various states are also in the process of implementing their own universal service programs. We are currently unable to quantify the amount of subsidy payments that we will be required to make to individual states. On July 30, 1999, the United States Court of Appeals for the Fifth Circuit overturned certain of the FCC's rules governing the basis on which the FCC collects subsidy payments from telecommunications carriers and recovery of those payments by incumbent local exchange carriers. In October 1999, on remand, the FCC issued new universal service rules. These or other changes to the universal service program could affect our costs. One or more parties may seek review of the new FCC rules by the Fifth Circuit and subsequently by the Supreme Court. The Fifth Circuit also remanded other rules to the FCC for further consideration.

TARIFFS AND RATES. In 1996, the FCC issued an order that required nondominant interexchange carriers, like us, to cease filing tariffs for our domestic interexchange services. The order required mandatory detariffing and gave carriers nine months to withdraw federal tariffs and move to contractual relationships with their customers. This order subsequently was stayed by a federal appeals court, and it is unclear at this time whether the detariffing order will be

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implemented. In June 1997, the FCC issued another order stating that nondominant local exchange carriers, like us, could withdraw their tariffs for interstate access services provided to long distance carriers. If the FCC's orders become effective, nondominant interstate services providers will no longer be able to rely on the filing of tariffs with the FCC as a means of providing notice to customers of prices, terms and conditions under which they offer their interstate services. If we cancel our FCC tariffs as a result of the FCC's orders, we may need to implement customer contracts, which could result in substantial administrative expenses.

In March 1999, the FCC adopted further rules that, while still maintaining mandatory detariffing, nonetheless require interexchange carriers to make specific public disclosures on their web sites of their rates, terms and conditions for domestic interstate services. The effective date for these rules is also delayed until a court decision on the appeal of the FCC's detariffing order.

JURISDICTIONAL NATURE OF INTERNET TRAFFIC. Recently, the FCC has determined that both continuous access and dial-up calls from a customer to an Internet service provider are interstate, not local, calls, and, therefore, are subject to the FCC's jurisdiction. The FCC has initiated a proceeding to determine the effect that this regulatory classification will have on the obligation of local exchange carriers to pay reciprocal compensation for dial-up calls to Internet service providers that originate on one local exchange carrier network and terminate on another local exchange carrier network. Moreover, several states are considering this issue, and several states have held that local exchange carriers do not need to pay reciprocal compensation for calls terminating at Internet service providers. On March 24, 2000, the Court of Appeals for the District of Columbia remanded for reconsideration the FCC's determination that calls to Internet service providers are interstate rather than local. Specifically, the Court indicated that the FCC has not provided a satisfactory explanation why calls to Internet service providers are not local telecommunications traffic and why such traffic is exchange access rather than telephone exchange service. We cannot predict the effect that the FCC's resolution of these issues will have on our business.

NUMBERING AND NUMBER PORTABILITY. In August 1997, the FCC issued rules transferring responsibility for administering and assigning local telephone numbers from the Bell operating companies and other incumbent local exchange carriers to a neutral entity in each geographic region in the United States. In August 1996, the FCC issued new numbering regulations that prohibit states from creating new area codes that could unfairly hinder competitive local exchange carriers by requiring their customers to use 10 digit dialing while existing incumbent local exchange carrier customers use seven digit dialing. In addition, each carrier is required to contribute to the cost of numbering administration through a formula based on net telecommunications revenues. Beginning in March 2000, contributions for this purpose will be based on end user telecommunications revenues and will be submitted in association with FCC Lifeline, Universal Service and the Schools and Libraries Funds.

In July 1996, the FCC released rules requiring all local exchange carriers to have the capability to permit both residential and business consumers to retain their telephone numbers when switching from one local service provider to another, known as "number portability." Number portability has been implemented in most of the areas in which we provide service, but has not been implemented everywhere in the United States. Some carriers have obtained waivers of the requirement to provide number portability, and others have delayed implementation by obtaining extensions of time before compliance is required. Lack of number portability in a given market could adversely affect our ability to attract customers for our competitive local

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exchange service offerings, particularly business customers, should we seek to provide services to such customers.

In May 1999, the FCC also initiated a proceeding to address the problem of the declining availability of area codes and phone numbers. Many of these numbering-related issues are subject to further change by the FCC and the courts, and could produce added administrative expenses for us.

RESTRICTIONS ON BUNDLING. Current FCC rules prohibit dominant carriers from bundling their non-competitive, regulated telecommunications services with their unregulated enhanced or information services. The Commission has never enforced this rule with respect to competitive local exchange carriers and has proposed eliminating the rule for all carriers.

SLAMMING. A customer's choice of local or long distance telecommunications company is encoded in a customer record, which is used to route the customer's calls so that the customer is served and billed by the desired company. A user may change service providers at any time, but the FCC and some states regulate this process and require that specific procedures be followed. When these procedures are not followed, particularly if the change is unauthorized or fraudulent, the process is known as "slamming." Slamming is such a significant problem that it has been addressed in detail by Congress in the Telecommunications Act, by some state legislatures, and by the FCC in recent orders. The FCC has levied substantial fines for slamming. The risk of financial damage and to business reputation from slamming is significant. Even one slamming complaint could cause extensive litigation expenses for us. The FCC recently decided to apply its slamming rules (which originally covered only long distance) to local service as well.

NETWORK INFORMATION. The Communications Act of 1934 and FCC rules protect the privacy of certain information about telecommunications customers that a telecommunications carrier such as us acquires by providing telecommunications services to such customers. Such protected information, known as Customer Proprietary Network Information (CPNI), includes information related to the quantity, technological configuration, type, destination and the amount of use of a telecommunications service. Under the FCC's rules, a carrier may not use the Customer Proprietary Network Information acquired through one of its offerings of telecommunications services to market certain other services without the approval of the affected customers. The United States Court of Appeals for the Tenth Circuit recently overturned the FCC's rules regarding the use and protection of Customer Proprietary Network Information. The FCC recently relaxed its customer proprietary network information rules somewhat, but it also has sought reconsideration of the Tenth Circuit decision. Further, FCC rules regarding handling of CPNI could result in significant administrative expense in modifying internal customer systems to meet such requirements.

OTHER ISSUES. There are a number of other issues and proceedings that could have an effect on our business in the future, including the fact that

- o The FCC has adopted rules to require telecommunications service providers to make their services accessible to individuals with disabilities, if readily achievable.

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- o The FCC has also ordered telecommunications service providers to provide law enforcement personnel with a sufficient number of ports and technical assistance in connection with wiretaps. We cannot predict the cost to us of complying with this order.
- o The FCC has adopted new rules designed to make it easier for customers to understand the bills of telecommunications carriers. These new rules establish certain requirements regarding the formatting of bills and the information that must be included on bills. These rules have been appealed in Federal court.
- o We are subject to annual regulatory fees assessed by the FCC, and must file an annual employment report to comply with the FCC's Equal Employment Opportunity policies.
- o The FCC has adopted an order granting limited pricing flexibility to large incumbent local exchange carriers, and is considering granting additional pricing flexibility and price deregulation options. These actions could increase competition for some of our services.

The foregoing is not an exhaustive list of proceedings or issues that could materially affect our business. We cannot predict the outcome of these or any other proceedings before the courts, the FCC, or state or local governments.

STATE REGULATION

To the extent that we provide telecommunications services which originate and terminate in the same state, we are subject to the jurisdiction of that state's public service commission. As our local service business and product lines expand, we will offer more intrastate service and may become increasingly subject to state regulation. The Telecommunications Act maintains the authority of individual state utility commissions to preside over rate and other proceedings, and to impose their own regulation on local exchange and intrastate interexchange services, so long as such regulation is not inconsistent with the requirements of federal law. For instance, states may require us to obtain a Certificate of Public Convenience and Necessity before commencing service in the state, and may impose tariff and filing requirements, consumer protection measures, and obligations to contribute to universal service and other funds. State commissions also have jurisdiction to approve negotiated rates, or establish rates through arbitration, for interconnection, including rates for unbundled network elements.

We are subject to requirements in some states to obtain prior approval for, or notify the state commission of, any transfers of control, sales of assets, corporate reorganizations, issuances of stock or debt instruments and related transactions. Although we believe such authorizations could be obtained in due course, there can be no assurance that state commissions would grant us authority to complete any of these transactions.

The Telecommunications Act generally preempts state statutes and regulations that restrict the provision of competitive services. As a result of this broad preemption, we will be generally free to provide the full range of local, long distance, and data services in any state. While this action greatly increases our potential for growth, it also increases the amount of

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competition to which we may be subject. States, however, may still restrict competition in some rural areas.

In particular, we expect to expand our Z-Line Home Edition service by starting to market this service in Pennsylvania by the end of the second quarter of 2000. We are currently offering service in New York via Bell Atlantic's tariffed offerings and in Massachusetts via a local interconnection agreement, dated December 30, 1999, between us and Bell Atlantic. Our service in Texas is provided via an interconnection agreement effective between us and Southwestern Bell Telephone Company, dated November 5, 1999. To effectuate service in Pennsylvania, we entered into a local interconnection agreement with Bell Atlantic on December 30, 1999. Under the terms of the agreements entered into with Bell Atlantic with respect to Massachusetts and Pennsylvania, Bell Atlantic will provide the unbundled network element platform components in a manner similar to that provided by Bell Atlantic in New York.

In order to enter new market areas, we may be required to negotiate interconnection contracts with incumbent local exchange carriers on an individual state basis. While current FCC rules and regulations require the incumbent provider to provide the network elements on an individual and combined basis necessary for us to provision end-user services, no assurance can be made that the individual local exchange providers will provide these components in a manner and at a price that will support competitive operations. If the incumbent providers do not readily provide network functionality in the manner required, we have regulatory and legal alternatives, including arbitration before state public service commissions, to force provision of services in a manner required to support our service offerings. However, if we are forced to litigate in order to obtain the combinations of network elements required to support our service, we are likely to incur significant incremental costs and delays in entering such markets.

LOCAL GOVERNMENT REGULATION

In some of the areas where we provide service, we may be subject to municipal franchise requirements requiring us to pay license or franchise fees either on a percentage of gross revenue, flat fee or other basis. We may be required to obtain street opening and construction permits from municipal authorities to install our facilities in some cities. The Telecommunications Act prohibits municipalities from discriminating among telecommunications service providers in imposing fees or franchise requirements. In some localities, the FCC has preempted fees and other requirements determined to be discriminatory or to effectively preclude entry by competitors, but such proceedings have been lengthy and the outcome of any request for FCC preemption would be uncertain.

EMPLOYEES

As of March 21, 2000, we had approximately 450 full-time employees, excluding approximately 31 individuals employed by a temporary employment service, some of whom we expect to offer full-time employment. None of our employees are covered under collective bargaining agreements, and we believe that our relationships with our employees are good.

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In connection with the deployment of our network architecture and the execution of our business plan, as well as the addition of Touch 1's personnel, if the acquisition is consummated, we believe that the number of our customer service, information systems installation and sales and marketing personnel will increase significantly.

ITEM 2. PROPERTIES

We currently lease our principal executive offices in Tampa, Florida and our principal engineering offices in Atlanta, Georgia.

ITEM 3. LEGAL PROCEEDINGS

We are a party to various routine administrative proceedings. For more information, please refer to the section entitled "Item 1. Business--Government Regulation."

In addition, in May 1998 we received a letter from Premiere Technologies, Inc. (Premiere), threatening legal action based on the allegation that our chief executive officer, Mr. Smith, a founder and a former director and executive vice president of Premiere, had, among other things, improperly used trade secrets belonging to Premiere in connection with the development of our technology. Although the parties have subsequently had some discussions and exchanged correspondence, including letters sent by Premiere to us in December 1999 reiterating prior claims and further discussions during which Premiere alleged the existence of additional intellectual property claims arising from the conduct of Mr. Smith, another one of our directors, one of our other officers and us, Premiere has never commenced any legal proceedings against us or Mr. Smith. While we believe that Premiere's alleged claims are without merit, we cannot assure you that Premiere will not try to pursue its claims through litigation or what the outcome of such litigation would be.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITIES HOLDERS

On or about October 8, 1999, a majority of our Series A and Series B preferred stockholders, respectively, approved, by written consent, an amendment to the Stockholders' Agreement by and among us, certain management personnel, and the Series A and Series B preferred stockholders that had the effect of adding the Series C preferred stockholder to the Stockholders' Agreement and altering certain rights of the Series B preferred stockholders. Series A preferred stockholders representing 1,078,318 shares of our Series A preferred stock and Series B preferred stockholders representing 2,140,477 shares of our Series B preferred stock approved the amendment pursuant to such written consent.

On or about October 30, 1999, a majority of our Series A preferred stockholders, Series B preferred stockholders and common stockholders, respectively, approved, by written consent, our 1998 Equity Participation Plan, adopted October 30, 1998, as amended (the Plan). Common stockholders representing 10,338,000 shares of our common stock, Series A preferred stockholders representing 1,078,318 shares of our Series A preferred stock and 343,588 shares of the Company's Series B preferred stock approved the Plan pursuant to such written consent.

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On November 23, 1999, we held a special meeting of our stockholders, at which our stockholders were requested to (1) approve an amendment to our articles of incorporation increasing the authorized shares to 200,000,000 shares, consisting of 150,000,000 shares of common stock, par value \$0.01 per share, and 50,000,000 shares of preferred stock, par value \$0.01 per share; and (2) approve an amendment to increase the number of shares subject to the Plan to 7,500,000. 14,657,017 votes were cast in favor of each proposal, with no votes cast against either of the proposals and no abstentions.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

The Company's Common Stock is traded on the Nasdaq National Market under the symbol "ZTEL."

The following table sets forth, for the periods indicated, the range of high and low closing sale prices for the Common Stock, as reported on the Nasdaq National Market since trading began on December 15, 1999, in connection with the Company's initial public offering, under the symbol ZTEL:

	HIGH	LOW
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CALENDAR YEAR 1999:		
Fourth Quarter (from December 15, 1999)	\$42.375	\$33.125
FISCAL YEAR 2000:		
First Quarter (through March 23, 2000)	\$47.25	\$25.8125

On March 23, 2000, the last reported sales price of the Common Stock on the Nasdaq National Market was \$42.25 per share. As of March 23, 2000, there were approximately 218 holders of record of the Common Stock.

We have not paid dividends on our common stock since our inception and do not intend to pay any cash dividends for the foreseeable future but instead intend to retain earnings, if any, for the future operation and expansion of our business. Any determination to pay dividends in the future will be at the discretion of our Board of Directors and will be dependent upon our results of operations, financial condition, restrictions imposed by applicable law and other factors deemed relevant by the Board of Directors.

USE OF PROCEEDS FROM INITIAL PUBLIC OFFERING

We filed a registration statement (Commission file no. 333-89063), which became effective on December 14, 1999, with respect to the initial public offering of 6,900,000 shares of our common stock (including the underwriters' over-allotment option). All 6,900,000 shares were sold, for an aggregate offering price of \$117,300,000. The offering was co-lead by joint-book running managers Thomas Weisel Partners LLC and Credit Suisse First Boston, and co-managed by J.C. Bradford & Co. and Stephens Inc.

From December 14, 1999 through December 31, 1999, the expenses incurred in connection with the offering were as follows: \$8,211,000 in underwriting discounts and commissions, \$1,693,000 in other expenses and \$9,904,000 in total expenses. The net offering proceeds after deduction of expenses were \$107,396,000. No expenses were paid, directly or indirectly, to our directors, officers, 10% shareholders or affiliates. Through December 31, 1999, approximately \$5,823,000

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of the net offering proceeds were used in the following estimated amounts and for the following purposes: \$1,398,000 for the purchase and installation of network equipment, \$1,041,000 for the purchase of software and support and software development, \$1,985,000 for marketing expenses, \$1,157,000 for operational expenses, and \$242,000 for construction of plant, building and facilities. The remaining \$99,234,000 has been placed in temporary investments in cash and cash equivalents. None of the net offering proceeds have been paid, directly or indirectly, to our directors, officers, 10% shareholders or affiliates.

RECENT SALES OF UNREGISTERED SECURITIES

During the period covered by this report, Z-Tel sold shares of its common stock in the amounts, at the times, and for the aggregate amounts of consideration listed below without registration under the Securities Act of 1933. Exemption from registration under the Securities Act for each of the following sales is claimed under Section 4(2) of the Securities Act because such transactions were by an issuer and did not involve a public offering:

On March 15, 1999, Z-Tel issued a warrant to purchase 521,832 shares of Common Stock to CMB Capital, LLC in connection with a \$35.2 million revolving sale-leaseback credit facility.

On September 22, 1999, Z-Tel issued, in the aggregate, 2,695,795 shares of Series B Preferred Stock to 53 persons for an aggregate consideration of \$10 million.

On October 8, 1999, Z-Tel issued 2,794,800 shares of Series C Preferred Stock to Gramercy Z-Tel, LLC for an aggregate consideration of \$15 million.

On October 13, 1999, Z-Tel issued 11,000 shares of common stock to Telebot Corporation in exchange for substantially all of its assets.

On October 13, 1999, Z-Tel issued 55,000 shares of common stock to Telutions LLC in connection with our purchase of software and support services.

On October 13, 1999, Z-Tel granted a warrant to purchase 115,500 shares of common stock to CMB Capital LLC in connection with an amendment to the existing facility, in which CMB Capital LLC agreed to, among other things, a provision for prepayment of the facility.

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ITEM 6. SELECTED CONSOLIDATED FINANCIAL DATA

The following selected historical consolidated financial data should be read in conjunction with the financial statements, related notes and other financial information contained in this document. You should also read "Management's Discussion and Analysis of Financial Condition and Results of Operations," contained later in this document. The Consolidated Statements of Operations Data for the year ended December 31, 1999 and the period from January 15, 1998 (Inception) through December 31, 1998, and the consolidated balance sheet data and other financial data as of December 31, 1999 and December 31, 1998, are derived from our financial statements that have been audited by our independent auditors.

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	YEAR ENDED DECEMBER 31, 1999	PERIOD JANUARY 15, 1998 (INCEPTION) THROUGH DECEMBER 31, 1998
<S>	<C>	<C>
Revenues	\$ 6,615,000	\$ 140,000
Operating expenses:		
Network operations	7,942,000	382,000
Sales and marketing	8,588,000	2,201,000
Research and development	3,562,000	4,728,000
General and administrative	15,379,000	4,718,000
Depreciation and amortization	4,372,000	1,283,000
Total operating expenses	39,843,000	13,312,000
Operating loss	(33,228,000)	(13,172,000)
Nonoperating income (expense):		
Interest income	608,000	228,000
Interest expense	(3,351,000)	(178,000)
Total nonoperating income (expense)	(2,743,000)	50,000
Net loss	(35,971,000)	(13,122,000)
Less mandatorily convertible redeemable preferred stock dividends	(1,654,000)	(190,000)
Net loss attributable to common stockholders	\$(37,625,000)	\$(13,312,000)
Weighted average common shares outstanding	15,099,359	6,554,499
Basic and diluted net loss per share	\$ (2.49)	\$ (2.03)

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CONSOLIDATED BALANCE SHEET DATA

Cash and cash equivalents	101,657,000	7,973,000
Working capital	95,315,000	3,328,000
Total assets	137,677,000	20,274,000
Total debt	14,134,000	724,000
Mandatorily convertible redeemable preferred stock	--	15,154,000
Total stockholder's equity (deficit)	114,378,000	(6,000)

OTHER FINANCIAL DATA

EBITDA (1)	(28,856,000)	(11,889,000)
Net cash used in operating activities	(32,681,000)	(7,769,000)
Net cash used in investing activities	(5,182,000)	(11,393,000)
Net cash provided by financing activities	131,547,000	27,135,000

(1) EBITDA consists of earnings before interest, income taxes, depreciation and amortization. While not a measure under generally accepted accounting principles, EBITDA is a measure commonly used in the telecommunications industry and is presented to assist in understanding our operating results. Although EBITDA should not be construed as a substitute for operating income (loss) determined in accordance with generally accepted accounting principles, it is included herein to provide additional information with respect to our ability to meet future debt service, capital expenditures and working capital requirements. The calculation of EBITDA does not include our commitments for capital expenditures and payment of debt and should not be deemed to represent our available funds. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" for a discussion of our financial operations and liquidity as determined in accordance with generally accepted accounting principles.

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion together with the "Selected Consolidated Financial Data," financial statements and related notes included in this document. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those projected in the forward-looking statements as a result of certain factors, including, but not limited to, those discussed in "Item 1. Business," as well as "Cautionary Statements Regarding Forward-Looking Statements," "Risks Related to our Financial Condition and our Business" and "Risks Related to our Industries," below, and other factors relating to our business and us that are not historical facts. Factors that may affect our results of operations include, but are not limited to, our limited operating history and cumulative losses, uncertainty of customer demand, rapid expansion, potential software failures and errors, potential network and interconnection failure, dependence on local exchange carriers, dependence on third party vendors, dependence on key personnel, uncertainty of government regulation, legal uncertainties, and competition. We disclaim any obligation to update information contained in any forward-looking statement.

OVERVIEW

We are an emerging provider of advanced, integrated telecommunications services targeted primarily to residential subscribers. For management purposes, we are organized into one reportable operating segment. We offer local and long distance telephone services in combination with enhanced communication features accessible through the telephone or the Internet. The nature of our business is rapidly evolving and we have a limited operating history. As a result, we believe that period-to-period comparisons of our revenues and operating results, including our network operations and other operating expenses as a percentage of total revenue, are not meaningful and should not be relied upon as indicators of future performance. We do not believe that our historical growth rates are indicative of future results.

REVENUES

We began offering Z-Line Home Edition service in New York in June 1999, Texas in December of 1999, and Massachusetts in March 2000. Z-Line Home Edition is our principal service offering. Z-Line Home Edition includes low-priced local and long-distance (1+) residential telephone services using a customer's existing telephone number, bundled with enhanced features, including caller identification, call forwarding, three-way calling, speed dialing, and dial-up remote access through our Z-Line Anywhere access card product, the full functionality of the Personal Communication Center (PCC) and, for an additional fee, Internet access. We expect sales and marketing expenses to increase substantially as we introduce our Z-Line Home Edition service into new markets. We intend to expand into Pennsylvania before the end of the second quarter of 2000. Our strategy will require us to hire additional sales and marketing personnel to build awareness of our services. We will also need to hire technical personnel to continue to expand our network architecture and enhance our service offerings. In addition to our internal technical staff, we expect to continue our relationship with third-party vendors and system integration consultants to integrate and enhance our customer care and

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billing software applications. We will continue to expand our network through leased facilities, strategic alliances, and acquisitions.

We began offering an access card service, similar to our current Z-Line Anywhere service, in the quarter ended December 31, 1998. Z-Line Anywhere is our access card product that allows a customer to make long-distance calls using Z-Tel's network from any phone simply by dialing a local access or toll-free 1-800 number. No change in phone service is required. Subscribers of Z-Line Anywhere also receive the full functionality of our PCC. Z-Line Anywhere is offered nationwide. Z-Line Anywhere customers are billed monthly in arrears, and the associated revenue is recognized in the month of service.

We began offering Z-Line Home Edition in June 1999. During 1999, we derived most of our revenue from service fees charged to Home Edition customers located in areas of New York served by Bell Atlantic. In addition to New York, we have begun to offer Z-Line Home Edition in Texas and Massachusetts and expect to offer this service in Pennsylvania before the end of the second quarter of 2000. We intend to offer the Z-Line Home Edition product throughout the United States, subject to the establishment, implementation, operation, and favorable pricing of the unbundled network elements by each state in accordance with the Telecommunications Act of 1996 and the more recent November 5, 1999 FCC order.

Charges for our Z-Line Home Edition basic services are billed in advance on a monthly basis. Long distance services in excess of a subscriber's basic package are billed in arrears. Revenue from Z-Line Home Edition is recognized as earned. Our Z-Line Home Edition customer agreements may be canceled on 30 days notice.

OPERATING EXPENSES

Operating expenses are comprised of:

- o network operations, which consists primarily of fixed and variable transmission expenditures, and rent expense for space in data centers;
- o sales and marketing, which consists primarily of telemarketing, advertising, sales compensation and related expenses;
- o research and development, which consists primarily of compensation and consulting fees related to the development of our proprietary technologies;
- o general and administrative, which consists primarily of compensation and related expenses, bad debt expense, occupancy costs and various administrative expenses; and
- o depreciation and amortization, which consists primarily of the non-cash reduction in carrying value of our long-lived assets.

We expect to expand our operations and workforce, including our network operations, technical support, sales, marketing and administrative resources. In particular, we intend to

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expand our existing sales force and create a locally based sales force in selected metropolitan areas where we intend to initiate service and determine a need for a physical sales presence. As a result, we expect to continue to incur substantial losses for the foreseeable future.

RESULTS OF OPERATIONS

Comparison of the year ended December 31, 1999 and the period January 15, 1998 (Inception) through December 31, 1998:

REVENUE. Revenue increased by \$6.5 million to \$6.6 million for the year ended December 31, 1999, compared to \$0.1 million for the period January 15, 1998 (Inception) through December 31, 1998. The following tables outline the approximate number of subscribers for Z-Line Home Edition and Z-Line Anywhere:

TYPE OF SERVICE	DECEMBER 31, 1999	DECEMBER 31, 1998
Z-LINE HOME EDITION SUBSCRIBERS	40,100	0
Z-LINE ANYWHERE SUBSCRIBERS	26,000	5,800

NETWORK OPERATIONS. Network operations expense increased by \$7.5 million to \$7.9 million for the year ended December 31, 1999, compared to \$0.4 million for the period January 15, 1998 (Inception) through December 31, 1998. The network operations expense primarily consists of transmission expenses for interconnection agreements with incumbent local exchange carriers (ILECs), service level agreements with inter-exchange carriers (IXCs), transmission services based on tariff arrangements, and employee salaries and benefits associated with the maintenance and operations of our networks. These various agreements include both fixed and variable line charges.

The increase in network operations expense was due primarily to growth in the number of subscribers resulting from the introduction of our Z-Line Home Edition services. We expect our network operations expense to increase significantly in future periods due to increases in subscribers.

SALES AND MARKETING. Sales and marketing expense increased \$6.4 million to \$8.6 million for the year ended December 31, 1999, compared to \$2.2 million for the period January 15, 1998 (Inception) to December 31, 1998. The sales and marketing expense primarily consists of telemarketing, development of our brand awareness through promotional and advertising materials, and employee salaries and benefits.

The increase in sales and marketing expense is attributable to our expanded sales and marketing efforts to increase our subscribers. We increased our telemarketing and advertising expenses in 1999 in connection with the introduction of our Z-Line Home Edition service. To

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meet the demands of our growth we increased our personnel in this department from approximately 10 at December 31, 1998 to approximately 20 at December 31, 1999. This increase is also attributable to the fact that marketing of our services did not begin in earnest until the fourth quarter of 1998. We intend to significantly increase our sales and marketing expenditures during the year 2000.

RESEARCH AND DEVELOPMENT. Research and development expenditures decreased \$1.1 million to \$3.6 million for the year ended December 31, 1999, compared to \$4.7 million, for the period January 15, 1998 (Inception) to December 31, 1998. Our research and development expenses consist primarily of software development costs and employee salaries and benefits. We adopted the provisions of Statement of Position (SOP) 98-1 "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use," at the beginning of 1999. As a result, \$4.8 million of our research and development costs relating to development of internal use software were capitalized for the year ended December 31, 1999, compared to \$0 for the period January 15, 1998 (Inception) through December 31, 1998.

In 1998, we expensed internal software development costs, as we were developing our Z-Line Anywhere and Z-Line Home Edition services and had not fulfilled the requirements for capitalization. The development of our Z-Line Home Edition, and the integration of our customer care and billing software required significant expenditures from employee compensation and outside consulting fees. These efforts were spent adding functionality and making significant enhancements to our technology. A portion of these services and purchases of software were capitalized in 1999 compared to 1998, as a result of the adoption of SOP 98-1 discussed in the prior paragraph, causing research and development expenses to decrease in 1999. We expect research and development costs to increase in the future as we improve and enhance our services.

GENERAL AND ADMINISTRATIVE. General and administrative expense increased \$10.7 million to \$15.4 million for the year ended December 31, 1999, compared to \$4.7 million for the period January 15, 1998 (Inception) to December 31, 1998. The increase in general and administrative expense was primarily due to increases in its primary components of employee salaries, temporary services, bad debt expense, and occupancy costs.

We increased the number of employees in general and administrative functions to 83 employees at December 31, 1999, from 22 employees at December 31, 1998. We increased our provision for bad debts during 1999, primarily because of our increase in subscribers for the year. We have implemented revised credit policies and are closely monitoring collection procedures to help minimize these expenses in the future. We have increased our leased facilities utilized to meet our increased personnel and growing need for infrastructure to support our current and future needs. We anticipate general and administrative expenditures will continue to increase in the future as we increase our services and enter new states to meet the demands of our anticipated growth.

DEPRECIATION AND AMORTIZATION. Depreciation and amortization expense increased \$3.1 million to \$4.4 million for the year ended December 31, 1999, compared to \$1.3 million for the period January 15, 1998 (Inception) through December 31, 1998. The increase was due to

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purchases of equipment, facilities, and the capitalized costs associated with internal software development totaling \$21.2 million for the year-ended December 31, 1999, compared to \$11.4 million for the period January 15, 1998 (Inception) through December 31, 1998. We expect depreciation and amortization to continue to increase significantly as we increase our capital expenditures.

INTEREST INCOME. Interest income increased \$0.4 million to \$0.6 million for the year ended December 31, 1999, compared to \$0.2 million for the period January 15, 1998 (Inception) through December 31, 1998. Interest income consists of income on our cash balances invested in short-term liquid investments. This increase was due primarily to the closing of two private securities offerings in 1999 and our initial public offering on December 15, 1999, which offering provided net proceeds of \$109.1 million after underwriting discount and commissions. These transactions in 1999 provided for larger cash balances compared to 1998. We anticipate that our interest income will continue to increase, as we will benefit from the interest earned from our initial public offering proceeds.

INTEREST EXPENSE. Interest expense increased \$3.2 million to \$3.4 million for the year ended December 31, 1999, compared to \$0.2 million for the period January 15, 1998 (Inception) through December 31, 1998. Our interest expense is a result of the interest charge on our capital lease obligations. The increase in our interest expense is primarily a result of our payments on the CMB Capital, LLC sale-leaseback agreement. We anticipate a reduction in the amount of interest expense in the future due to the extinguishment of our CMB Capital, LLC \$35.2 million revolving sale-leaseback credit facility on February 14, 2000.

INCOME TAX EXPENSE. No provision for federal or state income taxes has been recorded due to the full valuation allowance recorded against the deferred tax asset for the year ended December 31, 1999 and the period January 15, 1998 (Inception) through December 31, 1998.

NET LOSS. Our net loss increased \$22.9 million to \$36.0 million for the year ended December 31, 1999, compared to \$13.1 million for the period January 15, 1998 (Inception) through December 31, 1998. This increase was due primarily to the increases in expenses described above.

EBITDA. Many securities analysts use the measure of earnings before deducting interest, taxes, depreciation and amortization, also commonly referred to as "EBITDA," as a way of evaluating a company's financial performance. While EBITDA is not a measure under generally accepted accounting principles, EBITDA is a measure commonly used in the telecommunications industry and is presented to assist in understanding our operating results. Our negative EBITDA increased \$17.0 million to \$28.9 million for the year ended December 31, 1999, compared to \$11.9 million for the period January 15, 1998 (Inception) through December 31, 1998. We expect to experience increasing operating losses and negative EBITDA as result of our network development and the expansion of our markets and growth and expansion of operations.

LIQUIDITY AND CAPITAL RESOURCES

The competitive local telecommunications service business is traditionally considered to be a capital intensive business owing to the significant investments required in fiber optic communication networks and the collocation of switches and transmission equipment in incumbent local exchange carriers' central offices. Our network architecture is designed with remotely located points of presence, or Z-Nodes, that can be interconnected through local and long distance communications networks to the Z-Tel enterprise management center. We do not expect that the growth of our business will require the levels of capital investment in fiber optics and switches that existed in historical models. Instead, we will devote significant amounts of our capital resources to continued software development and to marketing efforts that we have designed to achieve rapid penetration of our target markets.

We have incurred significant accumulated losses since our inception as a result of developing our business, research and development, building and maintaining network infrastructure and technology, sales and promotion of our services, and administrative expenditures. As of December 31, 1999, we had an accumulated deficit of \$49.1 million and net operating loss carryforwards of \$49.3 million for tax purposes. We have funded these expenditures primarily through operating revenues, private securities offerings, a sale-leaseback credit facility and an initial public offering of 6.9 million shares of common stock (including the underwriters' over-allotment option) that raised net proceeds of \$109.1 million after underwriter discount and commissions. We intend to continue building our organization in anticipation of future growth and believe that our operating expenditures will also continue to increase. As of December 31, 1999, we had \$101.7 million in cash and cash equivalents.

NET CASH USED IN OPERATING ACTIVITIES. Net cash used in operating activities increased by \$24.9 million to \$32.7 million for the year ended December 31, 1999, compared to \$7.8 million for the period January 15, 1998 (Inception) through December 31, 1998. This net change in cash used in operating activities from year to year primarily was affected by increasing net losses, and was offset partially by non-cash charges associated with bad debt expense, depreciation, and expenses from the granting of stock options.

NET CASH USED IN INVESTING ACTIVITIES. Net cash used in investing activities decreased by \$6.2 million to \$5.2 million for the year ended December 31, 1999, compared to \$11.4 million for the period January 15, 1998 (Inception) through December 31, 1998. For the year ended December 31, 1999, we invested \$21.2 million in capital expenditures as compared to \$11.4 million in the period January 15, 1998 (Inception) through December 31, 1998. These purchases were primarily for the following items:

- o continued enhancement and improvement of our network;
- o employee compensation and outside consulting fees associated with the internal development and integration of our customer care and billing software; and
- o the build-out of our headquarters in Tampa, Florida.

The significant increase in capital expenditures is a direct result of our rapid growth in subscribers and the need to build and purchase infrastructure to support our current and future needs. In 1998, we focused on product development and the establishment of our infrastructure, the operation of our technology and a network that primarily involved the purchases of equipment for our Z-Nodes. As noted in the discussion regarding research and development, pursuant to our adoption of Statement of Position 98-1 as of January 1, 1999, we capitalized \$4.8 million of software development costs for the year ended December 31, 1999, compared to \$0 during the period January 15, 1998 (Inception) through December 31, 1998. Capitalized software development costs, in conjunction with capital outlays, contributed to the increased capital expenditures. On March 15, 1999, we entered into a \$35.2 million sale-leaseback facility agreement with CMB Capital, LLC to sell and lease back certain equipment, which provided \$16.0 million in cash from investment activities for the year ended December 31, 1999.

On February 14, 2000, we made a payment of \$14.4 million to extinguish the outstanding CMB Capital, LLC debt. This was the repayment of transactions involving the sale and leaseback of various furniture and equipment payable over four years from the date of the transactions. This transaction resulted in \$1.6 million of extraordinary loss, to be recorded in the first quarter of 2000, associated with the loss for the early extinguishment of debt and the expense relating to 115,500 stock warrants associated with the debt that was being expensed over the life of the lease. We expect cash used in investing activities to increase as we maintain and develop our network.

NET CASH PROVIDED BY FINANCING ACTIVITIES. Net cash provided by financing activities increased \$104.4 million to \$131.5 million for the year ended December 31, 1999, compared to \$27.1 million for the period January 15, 1998 (Inception) through December 31, 1999. The overall increase is primarily attributable to our initial public offering on December 15, 1999 of 6.9 million shares of common stock (including the underwriters' over-allotment options) for net proceeds of \$109.1 million after underwriter discount and commissions. Prior to our initial public offering, we raised \$10.0 million and \$15.0 million, respectively, through the offerings of our Series B and Series C preferred shares, compared with \$15.0 million raised through a Series A preferred stock offering in 1998. The net increase of cash provided by financing activities was reduced by the payments of our long-term debt and payments on our capital lease obligations, in the amounts of \$0.6 million and \$2.0 million, respectively, in 1999, compared to \$0.9 million and \$24,000, respectively, in 1998.

Our ongoing capital requirements will depend on several factors, including market acceptance of our services, the amount of resources we devote to investments in our networks, facilities, build-out of additional enterprise management centers, services development and brand promotions, the resources we devote to sales and marketing of our services, and other factors. We have experienced a substantial increase in our capital expenditures and operating losses since our inception consistent with the growth in our operations and staffing, and we anticipate that this will continue for the foreseeable future. Additionally, we expect to make additional investments in technologies and our network architecture, and plan to expand our sales and marketing programs and conduct more aggressive brand promotions. Although operating activities may provide cash in certain periods, to the extent we experience growth in the future, we anticipate that our operating and investing activities will use cash. Consequently, any such

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future growth will require us to obtain additional equity or debt financing which may not be available on attractive terms, or at all, or may be dilutive.

See "Item 1. Business--Acquisition of Touch 1 Communications, Inc." for a discussion of our planned acquisition of Touch 1 Communications, Inc.

IMPACT OF THE YEAR 2000

We did not experience any significant disruptions in its operations during the transition into the Year 2000. We believe we have completed necessary assessments, modifications or replacement and testing of systems critical for the delivery of our services. We believe our Year 2000 readiness objectives have been met. Because of these preparations, we did not experience any significant disruptions in our operations. We also prepared a contingency plan to mitigate potential adverse effects that might have arisen from non-compliant systems or third parties that had not adequately addressed the Year 2000 issue. While we did not experience any significant Year 2000 disruptions during the transition into the Year 2000, we will continue to monitor our operations and systems and address any date-related problems that may arise as the year progresses.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

The forward-looking statements in this document are based on the belief of our management, as well as assumptions made by and information currently available to our management. Forward-looking statements also may be included in other written and oral statements made or released by us. You can identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. The words "believe," "anticipate," "intend," "expect," "estimate," "project" and similar expressions are intended to identify forward-looking statements. Forward-looking statements describe our expectations today of what we believe is most likely to occur or may be reasonably achievable in the future, but they do not predict or assure any future occurrence and may turn out to be wrong. Forward-looking statements are subject to both known and unknown risks and uncertainties and can be affected by inaccurate assumptions we might make. Consequently, no forward-looking statement can be guaranteed. Actual future results may vary materially. We do not undertake any obligation to publicly update any forward-looking statements to reflect new information or future events or occurrences. These statements reflect our current views with respect to future events and are subject to risks and uncertainties about us, including, among other things:

- o our ability to market our services successfully to new subscribers;
- o our ability to access markets and finance network developments;
- o our enhancement and expansion;
- o additions or departures of key personnel;

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- o competition, including the introduction of new products or services by our competitors;
- o existing and future regulations affecting our business and our ability to comply with these regulations;
- o technological innovations;
- o general economic and business conditions, both nationally and in the regions in which we operate; and
- o other factors described in this document, including those described in more detail below.

We caution you not to place undue reliance on these forward-looking statements, which speak only as of the date of this document.

RISKS RELATED TO OUR FINANCIAL CONDITION AND OUR BUSINESS

LIMITED OPERATING HISTORY. We were formed in January 1998 and began offering telecommunications services to the public in September 1998. In addition, in June 1999, we began marketing our Z-Line Home Edition service in New York City and Long Island. We have had fewer than 17 months of actual marketing, sales and operational results. Our limited operating history and results make it very difficult to evaluate or predict our ability to, among other things, retain customers, generate and sustain a revenue base sufficient to cover our operating expenses, and to achieve profitability. As a result, we believe that our historical financial information is of little or no value in projecting our future results, making it even more difficult to evaluate our business and prospects.

UNCERTAIN DEMAND. We initially began to market our products and services in September 1998. In June 1999, we focused our product offering on sales of our Z-Line Home Edition service. Our products and services represent an emerging sector of the telecommunications industry, and the demand for our services and our ability to retain customers over time are highly uncertain. Consumer acceptance of our products and services could be limited by:

- o the willingness of customers to accept Z-Tel as an alternative provider of local and long distance telephone services and of other enhanced, integrated services;
- o the presence and attractiveness of other enhanced telecommunications service offerings in our target markets;
- o the perception of complexity in using our services;
- o the reliability of our technology and network infrastructure;

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- o the quality of our customer service; and
- o the prices of our services.

We have determined that substantial marketing effort, time and expense are required to stimulate initial demand for our products and services. In addition, we have incurred and will continue to incur substantial operating expenses, have made, and will continue to make, significant capital investments and have entered or plan to enter into real property leases, equipment supply contracts and service arrangements, in each case based upon our expectations as to the market acceptance of our products and services. We cannot be certain that substantial markets will develop for our products and services, or, if such markets develop, that we will be able to attract and maintain a sufficient revenue-generating customer base to cover our operating expenses. Lack of acceptance of our services in our target markets would materially and adversely affect the commercial viability of our business, and as a consequence, the value of your investment.

In addition, to maintain our competitive posture, we must be in a position to reduce the prices for our services in order to meet reductions in local and long distance rates, if any, offered by others. We cannot be sure that we will be able to match the reductions made by our competitors and, if we do, such reductions could have an adverse effect on our business, operating results and financial condition.

EXPECTATION OF FUTURE LOSSES. Our product and service offerings are at an early stage, and we cannot be sure that sales of our products or services will generate revenues sufficient to cover our operating expenses. Even if our products and services prove to be commercially successful, our operations may not become profitable. Starting up our company and developing our communications technology required substantial capital and other expenditures and further development of our business will require significant additional expenditures.

Since our inception in January 1998 through December 31, 1999, we have incurred accumulated losses of \$49.1 million. We expect to continue to have significant operating losses and retained losses and will record significant negative net cash flow before financing for the foreseeable future.

AVAILABILITY AND FAVORABLE PRICING OF UNBUNDLED NETWORK COMPONENTS. Our business strategy depends on a continued availability of unbundled network components and on existing and additional states maintaining and adopting favorable pricing rules for unbundled network components.

The public utilities commissions of certain states have adopted pricing rules for unbundled network components. As a result of these regulatory initiatives, the Bell operating companies operating in those states are required to offer to competitive local exchange carriers such as us, at forward-looking, long-run incremental cost-based prices, the facilities and equipment and the features, functions and capabilities of their local exchange network on an unbundled basis. We have recently commenced operations in New York, Texas and Massachusetts using unbundled network components. However, given that the FCC order

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permitting unbundled network components is subject to further appeal, we cannot be certain that unbundled network components will continue to be available in their present form in those states or other states or that such other states will ever adopt favorable unbundled network components pricing. Further regulatory changes may adversely affect unbundled network components or our Z-Line Home Edition strategy. Our business model is based, in part, on availability and favorable pricing of the unbundled network components, and any adverse changes in the unbundled network elements platform regulatory or competitive environment could have a material adverse effect on our business, financial condition and results of operations.

RAPID EXPANSION. We have rapidly expanded our operations since we were formed. We expect to grow our business rapidly in terms of the number of services we offer, the number of customers we serve and the regions we serve. We cannot assure you that we will successfully manage our efforts to:

- o expand, train, manage and retain our employee base;
- o expand and improve our customer service and support systems and improve the performance of billing systems;
- o introduce and market new products and services in addition to Z-Line Home Edition and our other service offerings;
- o enhance and upgrade the features of our software;
- o capitalize on new opportunities in the competitive marketplace; and
- o control our expenses.

The strains posed by these demands are magnified by the start-up nature of our operations. If we cannot manage our growth effectively, our results of operations could be adversely affected.

In order to increase our direct sales effort, we will need to significantly increase the size of our internal sales and marketing staff and will be required to obtain personnel who have experience in marketing services like ours. We cannot be certain that we will be able to identify and attract sufficient numbers of qualified personnel or that our sales and marketing organizations will successfully compete against the more extensive and well-funded sales and marketing organizations of many of our current and future competitors. Our inability to attract, recruit and retain sufficient or additional qualified personnel could have a material adverse effect on us.

DIFFICULTIES IN EXPANDING NETWORK INFRASTRUCTURE. We must continue to develop, expand and adapt our network infrastructure as the number of our users and the amount of information they wish to access and transfer increases and as our customers' demands change. We cannot be sure that we will be able to develop, expand or adapt the network infrastructure to meet additional demand or our customers' changing requirements on a timely basis, at a commercially

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reasonable cost, or at all. If we fail to expand our network infrastructure on a timely basis or adapt it to either changing customer requirements or evolving industry standards, these failures could cause our business to perform poorly.

ABILITY TO RESELL LONG DISTANCE SERVICES. We offer long distance telephone services as part of our service packages. We currently have agreements with various long distance carriers to provide transmission and termination services for all of our long distance traffic. These agreements generally provide for the resale of long distance services on a per-minute basis and contain minimum volume commitments. If we incur underutilization charges on rate increases, these charges or rate increases could adversely affect our operating results. In cases in which we have agreed to minimum volume commitments and fail to meet them, we will be obligated to pay underutilization charges.

RISK OF SOFTWARE FAILURES AND ERRORS. The software that we use and the software that we have developed internally and are continuing to develop may contain undetected errors. Although we have extensively tested our software, errors may be discovered in the software during the course of its use. Any errors may result in partial or total failure of our network, loss or diminution in service delivery performance, additional and unexpected expenses to fund further product development or to add programming personnel to complete or correct development, and loss of revenue because of the inability of customers to use our products or services, which could adversely affect our business condition.

PROTECTION OF PROPRIETARY TECHNOLOGY. We currently rely on a combination of copyright, trademark and trade secret laws and contractual confidentiality provisions to protect the proprietary information that we have developed. Our ability to protect our proprietary technology is limited, and we cannot assure you that our means of protecting our proprietary rights will be adequate or that our competitors will not independently develop similar technology. Also, we cannot be certain that the intellectual property that incumbent local exchange carriers or others claim to hold and that may be necessary for us to provide our services will be available on commercially reasonable terms. If we were found to be infringing upon the intellectual property rights of others, we might be required to enter into royalty or licensing agreements, which may be costly or not available on commercially reasonable terms. If successful, a claim of infringement against us and our inability to license the infringed or similar technology on terms acceptable to us could adversely affect our business.

DEPENDENCE ON INFORMATION SYSTEMS. Our billing, customer service and management information systems are newly developed and we may face unexpected system difficulties which would adversely affect our service levels and, consequently, our business.

Sophisticated information and processing systems are vital to our ability to monitor costs, render monthly invoices for services, process customer orders and achieve operating efficiencies. We rely on internal systems and third party vendors, some of which have a limited operating history, to provide our information and processing systems. If our systems fail to perform in a timely and effective manner and at acceptable costs, or if we fail to adequately identify all of our information and processing needs or if our related processing or information systems fail, these failures could have a material adverse effect on our business.

In addition, our right to use third party systems is dependent upon license agreements. Some of these agreements are cancelable by the vendor, and the cancellation or nonrenewal of these agreements could seriously impair our ability to process orders or bill our customers. As we continue to provide local telephone service, the need for sophisticated billing and information systems will also increase significantly and we will have significant additional requirements for data interface with incumbent local exchange carriers and others. We cannot be certain that we will be able to meet these additional requirements.

NETWORK FAILURE. The successful operation of our network will depend on a continuous supply of electricity at multiple points. Although the system that carries signals has been designed to operate under extreme weather conditions (including heavy rain, wind and snow), like all other telecommunications systems, our network could be adversely affected by such conditions. Our network, however, is equipped with a back-up power supply and our existing network operations center is equipped with both a battery back-up and an on-site emergency generator. If a power failure causes an interruption in our service, the interruption could negatively impact our operations.

Our network also may be subject to physical damage, sabotage, tampering or other breaches of security (by computer virus, break-ins or otherwise) that could impair its functionality. In addition, our network is subject to unknown capacity limitations that may cause interruptions in service or reduced capacity for our customers. Any interruptions in service resulting from physical damage or capacity limitations could cause our systems to fail.

NETWORK INTERCONNECTION. As a competitive provider of local telephone service, we must interconnect our network with the networks of incumbent local exchange carriers. We may not be able to obtain the interconnection we require at rates and on terms and conditions that permit us to offer services that are both competitive and profitable. In the event that we experience difficulties in obtaining high quality, reliable and reasonably priced services from other carriers, the attractiveness of our services is likely to be significantly impaired.

DEPENDENCE ON LOCAL EXCHANGE CARRIERS. We rely on incumbent local exchange carriers to supply key unbundled components of their network infrastructure to us on a timely and accurate basis, and in the quantities and quality demanded by us. We may from time to time experience delays or other problems in receiving unbundled services or facilities which we request, and there can be no assurance that we will be able to obtain such unbundled elements on the scale and within the time frames required by us. Any failure to obtain these components, services or additional capacity on a timely and accurate basis could adversely affect us.

ANTICIPATED CAPITAL NEEDS. If we expand more rapidly than currently anticipated or if our working capital needs exceed our current expectations, we may need to raise additional capital from debt or equity sources. If we cannot obtain financing on acceptable terms or at all, we may be required to modify, delay or abandon our current business plan, which is likely to materially and adversely affect our business and, as a result, the value of our common stock.

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DEPENDENCE ON THIRD PARTY VENDORS. We currently purchase the majority of our telecommunications equipment as needed from third party vendors, including Excel Switching Corporation, Sonus Networks, Inc., Dialogic Communications Corporation, Compaq Computer Corporation, and Sun Microsystems, Inc. In addition, we currently license our software from third party vendors, including Oracle Corporation, INPRISE Corporation, NOVERA Corp., and Netscape Communications, Inc. We typically do not enter into any long-term agreements with our telecommunications equipment or software suppliers. Any reduction or interruption in supply from our equipment suppliers or failure to obtain suitable software licensing terms could have a disruptive effect on our business and could adversely affect our results of operations.

DEPENDENCE ON MANAGEMENT AND KEY PERSONNEL. We depend on a limited number of key personnel who would be difficult to replace. If we lose the services of some of our key personnel, our business could suffer. We currently maintain a \$5,000,000 key man life insurance policy on the life of Mr. D. Gregory Smith, our president, chief executive officer and chairman of the board. We also depend on a limited number of key management, sales, marketing and product development personnel to manage and operate our business. In particular, we believe that our success depends to a significant degree upon our ability to attract and retain highly skilled personnel, including our engineering and technical staff. If we are unable to attract and retain our key employees, the value of our common stock could suffer.

RISKS RELATED TO OUR INDUSTRY

GOVERNMENT REGULATION AND LEGAL UNCERTAINTIES. We are subject to varying degrees of federal, state, and local regulation. In states where we will provide intrastate services, we generally will be subject to state certification or registration and tariff-filing requirements. Delays in obtaining the required state regulatory approvals may have a material adverse effect on our business. Challenges to our tariffs by third parties could cause us to incur substantial legal and administrative expenses.

We must also comply with various state and federal obligations that are subject to change, such as the duty to contribute to universal service subsidies, the impact of which we cannot yet fully assess. While we do not believe that compliance with federal and state reporting and regulatory requirements will be burdensome, our failure to do so may result in fines or other penalties being imposed on us, including loss of certification to provide services.

Decisions of the FCC and state regulatory commissions providing incumbent local exchange carriers with increased flexibility in how they price their services and with other regulatory relief, could have a material adverse effect on our business and that of other competitive local exchange carriers. Future regulatory provisions may be less favorable to competitive local exchange carriers and more favorable to their competitors. If incumbent local exchange carriers are allowed by regulators to lower their rates, engage in substantial volume and term discount pricing practices for their customers, or charge competitive local exchange carriers higher fees for interconnection to the incumbent local exchange carriers' networks, our business, operating results and financial condition could be materially adversely affected. Incumbent local exchange carriers may also seek to delay competitors through legal or regulatory challenges, or by recalcitrant responses to requirements that they open their markets

<PAGE>

through interconnection and unbundling of network elements. Our legal and administrative expenses may be increased because of our having to actively participate in rate cases filed by incumbent local exchange carriers, in which they seek to increase the rates they can charge for the unbundled network element platform components. Our profitability may be adversely affected if those carriers prevail in those cases. Pending court cases, in which certain provisions of the Telecommunications Act of 1996 will be conclusively interpreted, may increase the cost of unbundled network elements to us.

COMPETITION. The telecommunications and information services markets are intensely competitive and rapidly evolving. We expect competition to increase in the future. Many of our potential competitors have longer operating histories, greater name recognition, larger customer bases and substantially greater financial, personnel, marketing, engineering, technical and other resources than us. The principal competitive factors affecting our business operations will be price, the desirability of our service offering, quality and reliability of our services, innovation and customer service. Our ability to compete effectively will depend upon our ability to maintain high quality, market-driven services at prices generally equal to or below those charged by our competitors. This competition could materially adversely affect our business, financial condition and results of operations.

We face competition from a variety of participants in the telecommunications market. The largest competitor for local service in each market in which we compete is the incumbent local exchange carrier serving that market. Incumbent local exchange carriers have established networks, long-standing relationships with their customers, strong political and regulatory influence, and the benefit of state and federal regulations that, until recently, favored incumbent local exchange carriers. In the local exchange market, the incumbent local exchange carriers continue to hold near-monopoly positions. The long distance telecommunications market in which we compete has numerous entities competing for the same customers and a high average churn rate as customers frequently change long distance providers in response to the offering of lower rates or promotional incentives.

Prices in the long distance market have declined significantly in recent years and are expected to continue to decline. We will face competition from large interexchange carriers. Other competitors are likely to include incumbent local exchange carriers providing out-of-region (and, with the removal of regulatory barriers, in-region) long distance services, other incumbent local exchange carriers, other competitive local exchange carriers, cable television companies, electric utilities, wireless telephone system operators, microwave and satellite carriers and private networks owned by large end users.

The Telecommunications Act of 1996 facilitates such entry by requiring incumbent local exchange carriers to allow competing providers to acquire local services at wholesale prices for resale and to purchase unbundled network elements at cost-based prices. A continuing trend toward combinations and strategic alliances in the telecommunications industry, including potential consolidation among incumbent local exchange carriers or competitive local exchange carriers, or transactions between telephone companies and cable companies outside of the telephone company's service area, or between interexchange carriers and competitive local exchange carriers, could give rise to significant new competitors.

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The enhanced and information services markets are also highly competitive and we expect that competition will continue to intensify. Our competitors in these markets will include information service providers, telecommunications companies, on-line services providers and Internet service providers.

UNAUTHORIZED TRANSACTIONS; THEFT OF SERVICES. We may be the victim of fraud or theft of service. From time to time, callers have obtained our services without rendering payment by unlawfully using our access numbers and personal identification numbers. We attempt to manage these theft and fraud risks through our internal controls and our monitoring and blocking systems. If these efforts are not successful, the theft of our services may cause our revenue to decline significantly.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We currently have instruments sensitive to market risk relating to exposure to changing interest rates and market prices. We do not enter into financial instruments for trading or speculative purposes and do not currently utilize derivative financial instruments. Our operations are conducted primarily in the United States and as such are not subject to material foreign currency exchange rate risk.

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 short-term nature of the major portion of our investment portfolio.

<PAGE>

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA
Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

To the Board of Directors and Shareholders
Z-Tel Technologies, Inc. and Subsidiaries

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, changes in stockholders' equity (deficit) and cash flows present fairly, in all material respects, the financial position of Z-Tel Technologies, Inc. and its Subsidiaries at December 31, 1999 and 1998, and the results of their operations and their cash flows for the year ended December 31, 1999 and the period from January 15, 1998 (Inception) through December 31, 1998, in conformity with accounting principles generally accepted in the United States. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for the opinion expressed above.

PricewaterhouseCoopers LLP

Tampa, Florida
February 15, 2000

<PAGE>

Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 1999 AND 1998

<TABLE>
<CAPTION>

	1999	1998
ASSETS		
<S>	<C>	<C>
Current assets:		
Cash and cash equivalents	\$ 101,657,000	\$ 7,973,000
Accounts receivable, net of allowance for doubtful accounts of approximately \$408,000 at December 31, 1998 and \$54,000 at December 31, 1999	4,245,000	15,000
Prepaid expenses and other current assets	2,304,000	423,000
Total current assets	108,206,000	8,411,000
Property and equipment, net	28,549,000	11,710,000
Other	922,000	153,000
Total assets	\$ 137,677,000	\$ 20,274,000
LIABILITIES, MANDATORILY CONVERTIBLE REDEEMABLE PREFERRED STOCK AND STOCKHOLDERS' EQUITY (DEFICIT)		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 9,165,000	\$ 4,402,000
Current portion of long-term debt and capital lease obligations	3,726,000	681,000
Total current liabilities	12,891,000	5,083,000
Long-term debt and capital lease obligations	10,408,000	43,000
Total liabilities	23,299,000	5,126,000
Mandatorily convertible redeemable preferred stock, \$.01 par value; 50,000,000 shares authorized; 9,523,869 issued and outstanding (aggregate liquidation value of approximately \$15,154,000 at December 31, 1998)	--	15,154,000
Commitments and contingencies (Notes 6, 7 and 14)		
Stockholders' equity (deficit):		
Common stock, \$.01 par value; 150,000,000 shares authorized; 32,159,911 and 14,411,100 shares issued; 31,880,236 and 14,411,100 outstanding, respectively	322,000	144,000
Notes receivable from stockholders	(1,683,000)	(3,329,000)
Unearned stock compensation	(2,487,000)	(192,000)
Additional paid-in capital	167,637,000	16,493,000
Accumulated deficit	(49,093,000)	(13,122,000)
Treasury stock, 279,675 shares at cost	(318,000)	--
Total stockholders' equity (deficit)	114,378,000	(6,000)
Total liabilities, mandatorily convertible redeemable preferred stock and stockholders' equity (deficit)	\$ 137,677,000	\$ 20,274,000

</TABLE>

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

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

<TABLE>

<CAPTION>

	YEAR ENDED DECEMBER 31, 1999	PERIOD JANUARY 15, 1998 (INCEPTION) THROUGH DECEMBER 31, 1998
<S>	<C>	<C>
Revenues	\$ 6,615,000	\$ 140,000
Operating expenses:		
Network operations	7,942,000	382,000
Sales and marketing	8,588,000	2,201,000
Research and development	3,562,000	4,728,000
General and administrative	15,379,000	4,718,000
Depreciation and amortization	4,372,000	1,283,000
Total operating expenses	39,843,000	13,312,000
Operating loss	(33,228,000)	(13,172,000)
Nonoperating income (expense):		
Interest income	608,000	228,000
Interest expense	(3,351,000)	(178,000)
Total nonoperating income (expense)	(2,743,000)	50,000
Net loss	(35,971,000)	(13,122,000)
Less mandatorily convertible redeemable preferred stock dividends	(1,654,000)	(190,000)
Net loss attributable to common stockholders	\$(37,625,000)	\$(13,312,000)
Weighted average common shares outstanding	15,099,359	6,554,499
Basic and diluted net loss per share	\$ (2.49)	\$ (2.03)

</TABLE>

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

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY (DEFICIT)

<TABLE>
<CAPTION>

	COMMON STOCK		NOTES RECEIVABLE FROM STOCKHOLDERS	UNEARNED STOCK COMPENSATION	
	SHARES	PAR VALUE			
<S>	<C>	<C>	<C>	<C>	
Balances, January 15, 1998 (Inception)	--	\$ --	\$ --	\$ --	
Issuance of common stock	9,703,100	97,000	(3,329,000)		
Conversion of note payable and accrued interest to common stock	4,708,000	47,000			
Grant of stock options below intrinsic value				(281,000)	
Vesting of stock options granted below intrinsic value				89,000	
Accrued dividend on preferred stock					
Net loss					
Balances, December 31, 1998	14,411,100	144,000	(3,329,000)	(192,000)	
Issuance of common stock in Initial Public Offering, net of underwriter discount and commissions	6,900,000	69,000			
Cost of issuance of common stock in Initial Public Offering					
Issuance of common stock for exercise of stock options	306,555	3,000			
Issuance of common stock in exchange for services rendered	55,000	1,000			
Issuance of common stock to purchase assets	11,000				
Conversion of preferred stock to common stock	10,476,256	105,000			
Grant of stock options below intrinsic value				(3,225,000)	
Vesting of stock options granted below intrinsic value				930,000	
Treasury stock received upon cancellation of notes receivable from stockholder	(279,675)		318,000		
Repayment of stockholders' notes			1,222,000		
Forgiveness of stockholder's note			106,000		
Accrued dividend on preferred stock					
Net loss					
Balances, December 31, 1999	31,880,236	\$ 322,000	\$ (1,683,000)	\$ (2,487,000)	
		ADDITIONAL PAID-IN CAPITAL	ACCUMULATED DEFICIT	TREASURY STOCK	TOTAL STOCKHOLDERS' EQUITY (DEFICIT)
<S>	<C>	<C>	<C>	<C>	<C>
Balances, January 15, 1998 (Inception)	\$ --	\$ --	\$ --	\$ --	\$ --
Issuance of common stock	10,929,000				7,697,000
Conversion of note payable and accrued interest to common stock	5,473,000				5,520,000
Grant of stock options below intrinsic value	281,000				
Vesting of stock options granted below intrinsic value					89,000
Accrued dividend on preferred stock	(190,000)				(190,000)
Net loss			(13,122,000)		(13,122,000)
Balances, December 31, 1998	16,493,000		(13,122,000)	--	(6,000)
Issuance of common stock in Initial Public Offering, net of underwriter discount and commissions	109,020,000				109,089,000
Cost of issuance of common stock in Initial Public Offering	(1,693,000)				(1,693,000)
Issuance of common stock for exercise of stock options	535,000				538,000
Issuance of common stock in exchange for services rendered	299,000				300,000
Issuance of common stock to					

purchase assets	60,000			60,000
Conversion of preferred stock to common stock	39,809,000			39,914,000
Grant of stock options below intrinsic value	4,768,000			1,543,000
Vesting of stock options granted below intrinsic value				930,000
Treasury stock received upon cancellation of notes receivable from stockholder			(318,000)	--
Repayment of stockholders' notes				1,222,000
Forgiveness of stockholder's note				106,000
Accrued dividend on preferred stock	(1,654,000)			(1,654,000)
Net loss		(35,971,000)		(35,971,000)
Balances, December 31, 1999	\$ 167,637,000	\$ (49,093,000)	\$ (318,000)	\$ 114,378,000

</TABLE>

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

<TABLE>
<CAPTION>

	YEAR ENDED DECEMBER 31, 1999	PERIOD JANUARY 15, 1998 (INCEPTION) THROUGH DECEMBER 31, 1998
<S>	<C>	<C>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$ (35,971,000)	\$ (13,122,000)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization of fixed assets	4,372,000	1,283,000
Interest expense on capital lease obligation discount	2,192,000	--
Provision for bad debts	958,000	54,000
Expense charged for granting of stock options	387,000	89,000
Expense charged for granting of stock for services	300,000	--
Interest expense converted to common stock	--	170,000
Change in operating assets and liabilities:		
Increase in accounts receivable	(5,188,000)	(69,000)
Increase in prepaid expenses and other current assets	(1,881,000)	(423,000)
Increase in other assets	(769,000)	(153,000)
Increase in accounts payable and accrued liabilities	2,919,000	4,402,000
Total adjustments	3,290,000	5,353,000
Net cash used in operating activities	(32,681,000)	(7,769,000)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(21,151,000)	(11,393,000)
Proceeds from sale and leaseback transaction	15,969,000	--
Net cash used in investing activities	(5,182,000)	(11,393,000)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of notes payable	--	5,350,000
Proceeds from issuance of mandatorily convertible redeemable preferred stock	24,950,000	14,964,000
Proceeds from issuance of initial public offering, net underwriter discount and commissions	109,089,000	--
Payment of issuance cost of initial public offering	(1,693,000)	--
Proceeds from exercise of stock options	538,000	7,697,000
Proceeds from notes receivable	1,222,000	--
Payments on long-term debt obligations	(565,000)	(852,000)
Payments on capital lease obligations	(1,994,000)	(24,000)
Net cash provided by financing activities	131,547,000	27,135,000
Net increase in cash and cash equivalents	93,684,000	7,973,000
Cash and cash equivalents, beginning of period	7,973,000	--
Cash and cash equivalents, end of period	\$ 101,657,000	\$ 7,973,000
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	\$ 1,130,000	\$ 8,000
NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Property and equipment acquired under capital lease obligations	\$ 15,944,000	\$ 95,000
Property and equipment acquired with long-term debt	\$ --	\$ 1,505,000
Conversion of note payable and accrued interest to common stock	\$ --	\$ 5,520,000
Increase in additional paid-in capital for stock options granted	\$ 5,064,000	\$ 281,000
Net increase in unearned stock compensation for stock options granted	\$ 2,295,000	\$ 192,000
Accrued dividends on preferred stock	\$ 1,654,000	\$ 190,000
Notes receivable issued for common stock	\$ --	\$ 3,329,000
Forgiveness of note receivable issued for common stock	\$ (106,000)	\$ --
Common stock issued for purchase of assets	\$ 60,000	\$ --
Treasury stock received upon cancellation of note receivable for common stock	\$ (318,000)	\$ --
Conversion of preferred stock to common stock	\$ 39,914,000	\$ --

</TABLE>

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

<PAGE>

Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. NATURE OF BUSINESS

DESCRIPTION OF BUSINESS

Z-Tel Technologies, Inc. and subsidiaries ("Z-Tel" or the "Company") incorporated in Delaware on January 15, 1998 as Olympus Telecommunications Group, Inc. In March 1998, Olympus Telecommunications Group, Inc. changed its name to Z-Tel Technologies, Inc. The Company has seven wholly owned subsidiaries: Z-Tel Communications, Inc., Z-Tel Business Networks, Inc., Z-Tel Holdings, Inc., Z-Tel Communications of Virginia, Inc., Z-Tel, Inc., Z-Tel Network Services, Inc. and Tiger Acquisition Corporation. Z-Tel Technologies, Inc. is the parent company, and has no other operations. Z-Tel Communications, Inc. is the operating entity. The remaining subsidiaries have no significant operations.

Z-Tel is an emerging provider of advanced, integrated telecommunications services targeted primarily to residential subscribers. The Company offers local and long distance telephone services in combination with enhanced communication features accessible through the telephone or the Internet. The Company began offering an access card service in 1998, similar to the Company's current Z-Line Anywhere service. In addition, the Company began offering Z-Line Home Edition service in New York in June 1999, and Texas in December of 1999.

STOCK SPLIT

The Company's Board of Directors authorized an 11 for 10 stock split on November 19, 1999, which was effected in the form of a 10% stock dividend. All common share amounts have been adjusted to give effect to this split.

INITIAL PUBLIC OFFERING

On December 15, 1999, the Company filed its initial public offering (IPO) of 6,900,000 shares (including the underwriters' over-allotment option) of its common stock at \$17.00 per share. Net proceeds to the Company aggregated approximately \$109,089,000 after underwriter discount and commissions. All of the mandatorily convertible redeemable preferred stock outstanding at the date of the IPO was converted into 10,476,256 shares of common stock as of the closing date of the offering.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All material intercompany accounts and transactions have been eliminated.

CASH AND CASH EQUIVALENTS

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid expenses and other current assets consist primarily of prepaid maintenance and support contracts and advances to suppliers.

PROPERTY AND EQUIPMENT

Property and equipment are recorded at historical cost. Maintenance and repairs are expensed as incurred, while renewals and betterments are capitalized. Upon the sale or other disposition of property, the cost and related accumulated depreciation are removed from the accounts and any gain or loss is recognized in operations. Depreciation and amortization is provided on a straight-line basis over the following estimated useful lives:

	YEARS
Switching equipment	5
Computer equipment	5
Software	3
Furniture and office equipment	5-10
Leasehold improvements	3-10

ADOPTION OF NEW ACCOUNTING PRONOUNCEMENT

Effective January 1, 1999, the Company adopted Statement of Position (SOP) 98-1, "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use." SOP 98-1 requires computer software costs related to internal software that is incurred in the preliminary project stage to be expensed as incurred. When the capitalization criteria of SOP 98-1 have been met, costs of developing or obtaining internal-use computer software are capitalized. The Company capitalized approximately \$4,794,000 of internally developed software for the year ended December 31, 1999. Internal use software is included as a component of property and equipment on the consolidated balance sheet.

LONG-LIVED ASSETS

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net undiscounted cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the discounted cash flows. The Company has recognized no impairment losses.

INCOME TAXES

The Company utilizes the asset and liability method of accounting for income taxes. Under this method, deferred income taxes are recorded to reflect the tax consequences on future years of differences between the tax basis of assets and liabilities and their financial reported amounts at each year-end based on enacted laws and statutory rates applicable to the periods in which

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

differences are expected to affect taxable income. A valuation allowance is provided against the future benefits of deferred tax assets if it is determined that it is more likely than not that the future tax benefits associated with the deferred tax asset will not be realized.

STOCK-BASED COMPENSATION

The Financial Accounting Standards Board issued SFAS No. 123, "Accounting for Stock-Based Compensation." Under SFAS No. 123, entities recognize as expense, over the vesting period, the fair value of all stock-based awards on the date of the grant. The Company continues to apply the provisions of Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees," and provide pro forma net income and earnings per share disclosures for grants made as if the fair value method defined in SFAS No. 123 had been applied. The Corporation has elected to apply the provisions of APB Opinion No. 25 and consequently recognizes compensation expense over the vesting period for grants made to employees and directors only if, on the date of grant, the market price of the underlying stock option exceeds the exercise price. For stock options granted to non-employees, SFAS No. 123 requires entities to recognize as an expense, over the vesting period, the fair value of the options.

REVENUE RECOGNITION

Revenues are recognized when earned. Revenues related to long distance service charges are billed monthly in arrears and the associated revenues are recognized in the month of service. In June 1999, the Company began offering its local service, Z-Line Home Edition, to consumers. Charges for this service are billed monthly in advance and the Company recognizes revenues for this service ratably over the service period, which management believes approximates the actual provision of services.

ADVERTISING

Advertising costs are expensed as incurred. Included in sales and marketing expenses are advertising costs of approximately \$7,122,000 and \$592,000 for the year ended December 31, 1999 and the period January 15, 1998 (Inception) through December 31, 1998, respectively.

COSTS OF START-UP ACTIVITIES

The Company expenses the costs of start-up activities as incurred.

CONCENTRATIONS OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents and accounts receivable. The Company places its cash and cash equivalents in financial institutions considered by management to be high quality. The Company maintains cash balances at financial institutions in excess of the \$100,000 insured by the Federal Deposit Insurance Corporation (FDIC). The Company has approximately \$99 million invested in interest bearing money market and short-term fixed income investments that are not insured by the FDIC. The Company has not experienced any losses in these accounts and believes it is not exposed to any significant credit risk on cash balances. During the normal course of business, the Company extends credit to customers residing in the United States.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SEGMENT REPORTING

Statement of Financial Standards (SFAS) No. 131, "Disclosures about Segments of an Enterprise and Related Information," requires that the Company report financial and descriptive information about reportable segments, and how these segments were determined. The Company operated during fiscal year 1999 and the period January 15, 1998 (Inception) through December 31, 1998 in a single segment. The Company determines the allocation and performance of resources based on total operations. Based on these factors, management has determined that the Company operates as one segment as defined by SFAS No. 131.

FINANCIAL INSTRUMENTS

The recorded amounts of cash and cash equivalents approximate fair value due to the short-term nature of these instruments. The Company has determined that due to the interest rates and short-term nature of the capital lease obligation, the fair value approximates the value recorded.

MANAGEMENT'S USE OF 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 date of the financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

NEW ACCOUNTING PRONOUNCEMENTS

On November 24, 1999, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 100 ("SAB 100"), "Restructuring and Impairment Charges." SAB 100 provides the SEC staff's views regarding the accounting for and disclosure of certain expenses commonly reported in connection with exit activities and business combinations. The Company does not anticipate that SAB 100 will have a material impact on the consolidated financial statements.

On December 3, 1999, the SEC issued Staff Accounting Bulletin No. 101 ("SAB 101"), "Revenue Recognition in Financial Statements." While not intended to change current literature related to revenue recognition, SAB 101 provides additional guidance on revenue recognition policies and procedures. The Company believes that its current accounting policies and procedures related to revenue recognition comply with SAB 101.

RECLASSIFICATION

Certain amounts in the December 31, 1998 financial statements have been reclassified to conform with the December 31, 1999 presentation.

3. PROPERTY AND EQUIPMENT

At the respective dates, property and equipment consist of the following:

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

<TABLE>
<CAPTION>

	1999	1998
<S>	<C>	<C>
Switching equipment	\$11,018,000	\$ 6,672,000
Computer equipment	9,237,000	2,898,000
Software	10,820,000	2,984,000
Furniture and office equipment	1,078,000	254,000
Leasehold improvements	235,000	185,000
Construction-in-progress	1,815,000	
	-----	-----
	34,203,000	12,993,000
Less accumulated depreciation and amortization	5,654,000	1,283,000
	-----	-----
	\$28,549,000	\$11,710,000
	-----	-----

</TABLE>

Depreciation and amortization expense related to property and equipment amounted to approximately \$1,999,000 and \$2,373,000, respectively, for the year ended December 31, 1999 and approximately \$586,000 and \$697,000, respectively, for the period January 15, 1998 (Inception) through December 31, 1998.

At the respective dates, assets acquired under capital leases, included in property and equipment, consist of the following:

<TABLE>
<CAPTION>

	1999	1998
<S>	<C>	<C>
Switching equipment	\$10,778,000	\$ --
Computer equipment	4,868,000	--
Furniture and office equipment	298,000	95,000
	-----	-----
	15,944,000	95,000
Less accumulated depreciation and amortization	3,070,000	8,000
	-----	-----
	\$12,874,000	\$ 87,000
	-----	-----

</TABLE>

In March 1999, the Company entered into an agreement with CMB Capital, LLC (a wholly owned entity of a shareholder of the Company) to sell and lease-back certain equipment. This agreement allowed for a sale and lease-back of up to \$35.2 million of certain equipment with revolving terms of 48 months and approximate effective interest rates ranging from 10.0% to 19.5%. Included in this agreement was a stock warrant to purchase 521,832 shares of common stock at \$3.37 per share. The Company accounted for the warrant granted in accordance with SFAS No. 123, recognizing costs associated with the grant equal to the fair value of the warrant. The Company has recorded the fair value of the warrant as a commitment fee associated with the capital lease obligation and included it as part of minimum lease payments.

The warrant expires on March 2009. For the year ended December 31, 1999, the Company sold and leased-back certain equipment, receiving proceeds under this agreement of approximately \$16.0 million. No gain or loss was recognized on the sale of these assets. At December 31, 1999, the Company had approximately \$19.2 million available under this agreement for future sale and leaseback transactions. The assets of the Company collateralize these leases.

In November 1999, the Company entered into an agreement with CMB Capital, LLC to restructure the terms of the leasing facility to allow for the early payment of the facility. The

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Company granted warrants for 115,500 shares of common stock at \$7.27 per share. The Company repaid the entire facility subsequent to December 31, 1999, as described in Note 14.

4. OTHER ASSETS

At the respective dates, other assets consist of the following:

	1999	1998
Certificate of deposit, restricted	\$500,000	\$ --
Interest receivable from stockholders	205,000	85,000
Deposits	217,000	68,000
	-----	-----
	\$922,000	\$153,000
	=====	=====

The certificate of deposit is pledged as collateral on an outstanding letter of credit in the amount of \$500,000 related to lease obligations on one of the Company's office spaces.

5. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

At the respective dates, accounts payable and accrued liabilities consist of the following:

	1999	1998
Trade accounts payable	\$5,177,000	\$4,263,000
Deferred revenue	517,000	--
Accrued payroll and related liabilities	744,000	106,000
Dividend payable to preferred shareholders	1,844,000	--
Accrued rent	441,000	--
Other accrued liabilities	442,000	33,000
	-----	-----
	\$9,165,000	\$4,402,000
	=====	=====

6. LONG-TERM DEBT AND LEASES

LONG-TERM DEBT

During 1998, the Company financed the purchase of certain assets with a note payable. At December 31, 1999 and December 31, 1998, the balance of this note was approximately \$88,000 and \$653,000, respectively. The note bears interest at approximately 10.0% and is payable in the year 2000. The assets purchased collateralize the note.

OPERATING LEASES

The Company has entered into various non-cancelable operating leases for equipment and office space with monthly payments through the year 2009. Included in general and administrative expense is rental expense relating to operating leases of approximately \$1,606,000 and \$198,000 for the year ended December 31, 1999 and the period January 15, 1998 (Inception) through December 31, 1998, respectively.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

CAPITAL LEASES

The Company has entered into various capital lease obligations, with effective interest rates ranging from 10.0% to 19.5%, with monthly payments through the year 2003.

Future minimum lease payments under non-cancelable operating and capital leases and long-term debt as of December 31, 1999 are as follows:

<TABLE>
<CAPTION>

YEAR ENDING DECEMBER 31,	OPERATING LEASES	CAPITAL LEASE OBLIGATIONS	LONG-TERM DEBT
<S>	<C>	<C>	<C>
2000	\$ 1,004,000	\$ 5,285,000	\$ 88,000
2001	1,320,000	5,266,000	--
2002	1,183,000	5,247,000	--
2003	1,214,000	2,309,000	--
2004	1,256,000	--	--
	5,977,000	18,107,000	88,000
Less amount representing estimated executory costs (taxes, etc.), including profit thereon, included in total minimum lease payments	--	1,206,000	--
Net minimum payments	\$ 5,977,000	16,901,000	\$ 88,000
Less amount representing interest on obligations under capital lease		2,855,000	
Present value of minimum lease payments (including approximately \$3,638,000 due within one year)		\$ 14,046,000	

</TABLE>

As discussed in Note 14, On February 14, 2000 the Company paid \$14,365,000 in fulfillment of the capital lease obligations outstanding.

7. COMMITMENTS AND CONTINGENCIES

The Company has disputed billings and access charges from certain inter-exchange carriers (IXCs) and incumbent local exchange carriers (ILECs). The Company contends the invoicing of billings and access charges are not in accordance with the interconnection, service level, or tariff agreements entered between the Company and certain IXCs and ILECs. The Company has not paid for a portion of these disputes and management believes that the Company will prevail in these disputes. At December 31, 1999, the disputed amounts recognized were approximately \$2,300,000.

The Company is involved in certain legal actions and claims arising in the ordinary course of its business. It is the opinion of management that such litigation and claims will be resolved without material adverse effect on the Company's financial position, results of operations, or cash flows. The Company is also aware of a threatened claim from a third party primarily involving allegations of improper use of trade secrets. No legal action has commenced related to this alleged claim, which the Company believes is without merit. Should any legal action result, the Company intends to vigorously defend its position.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

8. INCOME TAXES

For the year ended December 31, 1999 and the period January 15, 1998 (Inception) through December 31, 1998, no benefit for federal or state income taxes has been recorded due to the full valuation allowance recorded against the deferred tax asset.

As of December 31, 1999 and 1998, the Company had a net operating loss of approximately \$49,320,000 and \$12,700,000, respectively, available to reduce future federal income taxes. This net operating loss carryforward will begin to expire in 2018 and is subject to limitation in any given year in the event of certain changes in ownership, as set forth in the Internal Revenue Code Section 382 and related Treasury Regulations.

The tax effect of the temporary differences that gave rise to the deferred tax balances at the respective dates were the following:

	1999	1998
Current deferred tax assets:		
Accounts receivable	\$ 155,000	\$ 20,000
Noncurrent deferred tax assets:		
Net operating loss	18,742,000	4,827,000
Fixed assets	(876,000)	70,000
Deferred compensation	295,000	34,000
Other	292,000	22,000
	18,453,000	4,953,000
Deferred tax assets	18,608,000	4,973,000
Valuation allowance	(18,608,000)	(4,973,000)
	\$ --	\$ --

The Company provides a valuation allowance against net deferred tax assets if, based on the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. The net deferred tax asset at December 31, 1999 and 1998 has been offset by the establishment of a valuation allowance for the full amount of the deferred tax asset.

The following table summarizes, at the respective dates, the approximate differences between the actual tax provision and amounts obtained by applying the statutory U.S. federal income tax rate of 35% to the income (loss) before income taxes.

	1999	1998
Statutory provision/(benefit)	\$(12,590,000)	\$ (4,592,000)
State taxes net of federal provision/(benefit)	(1,045,000)	(381,000)
	(13,635,000)	(4,973,000)
Change in valuation allowance	13,635,000	4,973,000
	\$ --	\$ --

9. COMMON STOCK

In connection with the closing of the IPO, the Company amended its Articles of Incorporation to provide the authority to issue 150,000,000 shares of common stock and 50,000,000 shares of preferred stock, both with a \$.01 par value.

No dividends on common stock have been declared by the board of directors since January 15, 1998 (Inception).

10. MANDATORILY CONVERTIBLE REDEEMABLE PREFERRED STOCK

During 1998, the Company amended its articles of incorporation to authorize the issuance of up to 5,930,749 shares of Series A mandatorily convertible redeemable preferred stock (Series A Preferred) and 1,338,208 shares of Series B mandatorily convertible redeemable preferred stock (Series B Preferred), both with a \$.01 par value.

In November 1998, the Company closed a private placement of 2,695,795 shares of Series A Preferred and 1,338,208 shares of Series B Preferred, receiving aggregate net proceeds of approximately \$15 million.

During 1999, the Company amended its articles of incorporation to reduce the authorized shares of its Series A Preferred from 5,930,749 to 2,695,795 and increase the authorized shares of its Series B Preferred from 1,338,208 to 4,034,003. In September 1999, the Company closed a private placement of 2,695,795 shares of Series B mandatorily convertible redeemable preferred stock. The Company received aggregate net proceeds of approximately \$10 million from this placement.

In October 1999, the Company amended its articles of incorporation to authorize the issuance of up to 2,794,800 shares of its Series C mandatorily convertible redeemable stock (Series C Preferred). The Company closed a private placement of 2,794,800 shares of Series C Preferred stock. The Company received aggregate net proceeds of approximately \$15 million from this placement.

The preferred stock issues yielded 8% cumulative dividends, which amounted to approximately \$1,654,000 and \$190,000 at December 31, 1999 and 1998, respectively. In January of 2000, the Company paid approximately \$1,844,000 to the preferred shareholders in satisfaction of the 8% cumulative dividend as all shares were converted to common stock.

In December 1999, in connection with the closing of the Company's IPO, all of the mandatorily convertible redeemable preferred stock outstanding was converted into 10,476,256 shares of common stock.

In 1998 and 1999, the Company did not comply with certain provisions of the Series A Preferred private placement agreement relating to the issuance of financial statements to the stockholders within a certain time frame. The Company obtained a waiver from the stockholders relating to

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

these provisions in 1998. In December 1999, these provisions and a put agreement expired as a result of the conversion of the Series A and B Preferred to common stock.

11. RELATED PARTY TRANSACTIONS

During 1998, various executives of the Company issued full recourse promissory notes, totaling approximately \$3.3 million, to the Company in connection with the purchase of 2,929,575 shares of common stock. The accompanying consolidated financial statements include the notes as a decrease in stockholders' equity. The outstanding notes receivable at December 31, 1999 and 1998 are approximately \$1,683,000 and \$3,329,000, respectively. The principal balance of the notes and the related accrued interest (8% per annum) are due December 31, 2001. The notes are collateralized by the shares of common stock acquired with the notes, and those shares are held in escrow by the Company. Interest income on these notes receivable was \$251,000 and \$85,000 in 1999 and 1998, respectively.

During 1998, an executive loaned the Company approximately \$5.35 million with interest at a rate of 8% per year until paid. In August 1998, the Company issued 4,708,000 shares of common stock to the executive in satisfaction of the debt and accrued interest payable of \$170,000.

In September 1999, the Company cancelled approximately \$318,000 of notes receivable and reacquired 279,675 shares of common stock at \$1.14 per share from an employee. At December 31, 1999, these shares are presented as treasury shares, at cost.

12. STOCK-BASED COMPENSATION

Effective October 30, 1998, the Company adopted the 1998 Equity Participation Plan (the Plan) available for grant to eligible employees and eligible participants to purchase up to 1,261,000 shares of the Company's common stock. During September and November 1999, the board of directors (the Board) increased the shares available for grant under the Plan to 6,000,000 and 7,500,000, respectively. The Plan is administered by a committee appointed by the Board, or by the Board. The Board or the appointed committee shall administer the Plan, select the eligible employees and eligible participants to whom options will be granted, the price to be paid, the exercise period and the number of shares subject to any such options and interpret, construe and implement the provisions of the Plan.

During the year ended December 31, 1999 and the period January 15, 1998 (Inception) through December 31, 1998, respectively, the Company awarded options under the Plan totaling 3,829,557 and 201,850 shares of common stock, respectively, at a weighted average option price per share of \$5.49 and \$3.64. Stock option grants approximate the fair market value at the date of grant. The vesting periods on these options range from immediately to four years and have a maximum contractual life of ten years.

Prior to the adoption of the Plan, the Board issued stock options (the Initial Plan) totaling 3,878,050 shares to various parties at a weighted average option price per share of \$2.83. The vesting periods on these options range from immediately to three years, and have a maximum contractual life of ten years.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A summary of the stock option activity for the year ended December 31, 1999 and the period January 15, 1998 (Inception) through December 31, 1998 is presented below:

<TABLE>
<CAPTION>

	INITIAL PLAN		1998 EQUITY PARTICIPATION PLAN		TOTAL	
	NUMBER OF SHARES	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER OF SHARES	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER OF SHARES	WEIGHTED AVERAGE EXERCISE PRICE
<S>	<C>	<C>	<C>	<C>	<C>	<C>
OUTSTANDING, JANUARY 15, 1998 (INCEPTION)	--	\$ --	--	\$ --	--	\$ --
Granted	3,878,050	2.83	201,850	3.64	4,079,900	2.87
Forfeited	(58,850)	2.46	--	--	(58,850)	2.46
OUTSTANDING, DECEMBER 31, 1998	3,819,200	2.79	201,850	3.64	4,021,050	2.83
Granted			3,829,557	5.49	3,829,557	5.49
Exercised	(305,088)	1.73	(1,467)	3.64	(306,555)	1.74
Forfeited	(331,973)	3.49	(55,795)	3.69	(387,768)	3.52
OUTSTANDING, DECEMBER 31, 1999	3,182,139	\$ 2.87	3,974,145	\$ 5.42	7,156,284	\$ 4.29

</TABLE>

Had compensation cost for the Company's stock options granted been determined based on the fair value at the date of grant, consistent with the provisions of SFAS No. 123, the Company's net loss and loss per share of common stock for the year ended December 31, 1999 and the period January 15, 1998 (Inception) through December 31, 1998, respectively, would have been increased to the pro forma amounts shown below.

<TABLE>
<CAPTION>

	YEAR ENDED	PERIOD
	DECEMBER 31, 1999	JANUARY 15, 1998 (INCEPTION) THROUGH DECEMBER 31, 1998
<S>	<C>	<C>
NET LOSS		
As presented	\$(35,971,000)	\$(13,122,000)
As adjusted	(36,477,000)	(13,161,000)
BASIC AND DILUTED NET LOSS PER COMMON SHARE		
As presented	\$ (2.49)	\$ (2.00)
As adjusted	(2.42)	(2.01)

</TABLE>

These adjusted amounts were determined using the Black-Scholes valuation model with the following key assumptions: (a) a discount rate ranging from approximately 5% to 6%, (b) a volatility factor of 81%; (c) an average expected option life of 5 years; (d) there have been no options that have expired; and (e) no payment of dividends on common stock.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

During 1999 and 1998, respectively, included in the options and warrants granted by the Company, are 695,082 and 113,300 options granted to non-employees. The Company recorded expense for the same periods, respectively, of approximately \$311,000 and \$89,000 related to these non-employee options in accordance with the provisions of SFAS No. 123.

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

EXERCISE PRICES	NUMBER OUTSTANDING	WEIGHTED AVERAGE REMAINING CONTRACTUAL LIFE (IN YEARS)	NUMBER EXERCISABLE
\$1.14 - \$3.64	5,515,414	8.7	2,583,795
\$5.45 - \$7.27	1,149,720	9.8	148,500
\$10.00 - \$15.45	367,150	9.8	--
\$17.00 - \$39.00	124,000	10.0	--
	7,156,284		2,732,295

13. COMPUTATION OF NET LOSS PER SHARE

Basic net loss per share is computed by dividing net loss attributable to common stockholders by the weighted average number of common shares outstanding during the period. Diluted net loss per share assumes the exercise of common stock equivalents for which market price exceeds exercise price, less shares assumed purchased by the Company with related proceeds. Incremental shares of common stock equivalents are not included in the calculation of net loss per share as the inclusion of such equivalents would be anti-dilutive.

Net loss per share is calculated as follows:

<TABLE>

<CAPTION>

	YEAR ENDED DECEMBER 31, 1999	PERIOD JANUARY 15, 1998 (INCEPTION) THROUGH DECEMBER 31, 1998
	<C>	<C>
BASIC AND DILUTED NET LOSS PER SHARE:		
Loss attributable to common stockholders:		
Net loss	\$(35,971,000)	\$(13,122,000)
Less mandatorily convertible redeemable preferred stock dividends	(1,654,000)	(190,000)
Loss attributable to common stockholders	\$(37,625,000)	\$(13,312,000)
Weighted average common shares outstanding	15,099,359	6,554,499
Basic and diluted net loss per share	\$ (2.49)	\$ (2.03)

</TABLE>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For each of the periods presented, basic and diluted net loss per share are the same. Unexercised options to purchase 7,156,284 and 4,021,051 shares of common stock and mandatorily convertible redeemable preferred stock convertible into 0 and 4,437,403 shares of common stock for the year ended December 31, 1999 and the period January 15, 1998 (Inception) through December 31, 1998, respectively, which could potentially dilute basic earnings per share in the future were not included in the computation of diluted net loss per share for these periods because to do so would have been antidilutive in each case.

14. SUBSEQUENT EVENTS

On January 24, 2000, the Company entered into an agreement in principle to acquire Touch 1 Communications, Inc. (Touch 1), a provider of long-distance and telemarketing services. In addition to entering this agreement, the Company formed a new subsidiary, Tiger Acquisition Corporation, for the purposes of executing this pending acquisition. The acquisition of Touch 1 will be accounted for using the purchase method of accounting. The purchase price and acquisition are subject to, among other things, the signing of a definitive agreement, regulatory approvals, and customary closing conditions. The acquisition of Touch 1 is expected to be completed by the end of May 2000.

On February 14, 2000, the Company paid CMB Capital, LLC approximately \$14,366,000 to extinguish the outstanding debt relating to the sale and leaseback of its \$35.2 million revolving credit facility. As a part of this transaction, the Company will recognize an extraordinary loss of approximately \$1,600,000. The extraordinary loss consists of the expense to extinguish the debt and the unamortized portion of 115,500 stock warrants issued pursuant to the agreement that were being amortized over the life of the debt.

15. QUARTERLY OPERATING RESULTS (UNAUDITED)

The following table presents unaudited quarterly operating results for each of the last seven quarters, as this table includes all full quarters of operations since inception on January 15, 1998. This information has been prepared by the Company on a basis consistent with the Company's consolidated financial statement statements and includes all adjustments, consisting only of normal recurring accruals, in accordance with generally accepted accounting principles. Such quarterly results are not necessarily indicative of future operating results.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

QUARTER ENDED

	JUNE 30, 1998	SEPTEMBER 30, 1998	DECEMBER 31, 1998
	-----	-----	-----
Sales	\$ --	\$ --	\$ 140,000
Operating loss	2,641,000	3,833,000	6,437,000
Net Loss	(2,716,000)	(3,850,000)	(6,161,000)
Loss per share (1)	\$ (1.13)	\$ (0.63)	\$ (0.44)
Weighted average shares outstanding	2,403,500	6,230,098	14,411,100

<TABLE>

<CAPTION>

QUARTER ENDED

	MARCH 31, 1999	JUNE 30, 1999	SEPTEMBER 30, 1999	DECEMBER 31, 1999
	-----	-----	-----	-----
<S>	<C>	<C>	<C>	<C>
Sales	\$ 664,000	\$ 761,000	\$ 745,000	\$ 4,445,000
Operating loss	5,843,000	4,488,000	10,849,000	16,493,000
Net loss	(5,939,000)	(5,611,000)	(12,097,000)	(12,324,000)
Loss per share (1)	\$ (0.43)	\$ (0.41)	\$ (0.96)	\$ (0.75)
Weighted average shares outstanding	14,411,000	14,411,000	13,025,563	17,257,893

</TABLE>

(1) Earnings per share were calculated for each three month and twelve month period on a stand-alone basis.

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ITEM 9. DISAGREEMENTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

DIRECTORS AND EXECUTIVE OFFICERS

The following sets forth certain information regarding our directors and executive officers as of March 23, 2000:

<TABLE>

<CAPTION>

NAME	AGE	POSITION
----	---	-----
<S>	<C>	<C>
D. Gregory Smith	40	President, Chief Executive Officer and Chairman of the Board and Director
David J. Malfara, Sr.	45	President, Z-Tel Network Services, Inc.
John M. Hutchens	52	Senior Vice President--Chief Financial Officer
Charles W. McDonough	48	Senior Vice President--Chief Technology Officer
J. Bryan Bunting	53	Senior Vice President--Engineering and Technical Support
James A. Kitchen	40	Senior Vice President--Chief Architect
N. Dumas Garrett	39	Senior Vice President--Business Development
Mark H. Johnson	43	Secretary and Treasurer
Jeffrey H. Kupor	31	General Counsel
Andrew L. Graham	42	Chief Legal Officer
Robert A. Curtis	32	Senior Vice President--Strategic Planning
Doug W. Jackson	34	Vice President--Marketing
Eduard J. Mayer	47	Director and Vice President--Strategic Alliances
Douglas C. Williamson	48	Director
Jeffrey A. Bowden	55	Director
Buford H. Ortale	38	Director
Laurence S. Grafstein	39	Director

</TABLE>

D. Gregory Smith, a founder of Z-Tel, has served as chairman of the board and chief executive officer of Z-Tel since inception. Mr. Smith was a director of Premiere Technologies, Inc. from 1991 to 1997, executive vice president from 1994 to 1997 and vice president from 1991 to 1994. From 1987 to 1991, Mr. Smith was a management and financial consultant with Olympus Telecommunications, Inc. and Olympus Partners, Inc., companies that he founded. Mr. Smith has also held positions with NationsBank of Florida, N.A. and Chase Bank of Florida. Mr. Smith received his B.S. in Commerce from the University of Virginia.

David J. Malfara, Sr. has served as president of Z-Tel Network Services, Inc. since February 1999. Mr. Malfara has over twenty-four years of telecommunications experience. He founded and sold Pace Long Distance Service and Pace Network Services. He has previously served as vice president of engineering at National Computer Corporation, as technical advisor/telecommunications at Honeywell Information Systems and as senior engineer at GTE Telenet.

John M. Hutchens has served as senior vice president--chief financial officer since September 1999. From 1982 through 1999 he was an employee and then a partner at Arthur Andersen LLP. Mr. Hutchens received a B.S. in Accountancy from the University of Illinois, and

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a Masters of Health Administration from the Ohio State University. Mr. Hutchens is a Certified Public Accountant licensed in Florida.

Charles W. McDonough has served as senior vice president--chief technology officer since August 1998. From 1975 through 1998, he was an employee and then a partner at Andersen Consulting LLP. Mr. McDonough received a B.A. in Industrial Engineering and a M.S. in Industrial Administration from Carnegie Mellon University.

J. Bryan Bunting has served as senior vice president--engineering and technical services since January 1999. Mr. Bunting served as senior vice president--Z-Tel Business Networks from August 1998 to January 1999. From 1968 through 1998, he was an officer of NationsBank, serving most recently as senior vice president of direct banking. Mr. Bunting attended Old Dominion University.

James A. Kitchen, a founder of Z-Tel, has served as senior vice president--chief architect of Z-Tel since January 1999. He served as vice president, engineering from January 1998 to December 1998 and was a chief architect and developer of Premiere Communications, Inc. from 1992 to 1997. Mr. Kitchen received his B.S. in Engineering from Georgia Institute of Technology.

N. Dumas Garrett has served as senior vice president--business development of Z-Tel since December 1999. From 1987 through 1999, he was an officer of Stephens, Inc., serving most recently as managing director and senior vice president and head of the technology and telecommunications group. Mr. Garrett has a B.S. in Industrial Engineering from the University of Arkansas and an M.B.A. from the University of Virginia.

Mark H. Johnson has served as secretary and treasurer of Z-Tel since August 1999. From May 1998 until his arrival at Z-Tel, Mr. Johnson was an employee of Olympus Management, a venture firm. From November 1991 until May 1998, Mr. Johnson was a credit policy executive of First Union National Bank. Mr. Johnson holds a B.A. from the University of Virginia.

Jeffrey H. Kupor has served as general counsel of Z-Tel since November 1999. From September 1993 until January 1998, Mr. Kupor was an attorney with the Houston office of Fulbright & Jaworski LLP, specializing in complex commercial and securities litigation. From January 1998 until November 1999 Mr. Kupor was a Staff Attorney and later Counsel at A I M Management Group, Inc., an investment adviser to a group of registered investment companies, where his responsibilities included securities registration, corporate and fund litigation, and labor and employment-related legal issues. Mr. Kupor has a B.S. in Economics from the University of Pennsylvania and a J.D. from the Boalt Hall School of Law at the University of California at Berkeley.

Andrew L. Graham has served as chief legal officer of Z-Tel since September 1999. He has practiced corporate and tax law in Tampa, Florida since 1988, most recently with the firm of Cass & Graham. He earned his Bachelor's in accounting from Florida State University and his law degree, with honors, from the University of Florida College of law in 1987 and went on to earn a Master of Laws in Taxation there in 1988.

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Robert A. Curtis has served as senior vice president--strategic planning since July 1999. From May 1998 to June 1999, Mr. Curtis was vice president--business development and legal affairs at Z-Tel. From September 1995 to April 1998, Mr. Curtis was an attorney at the Houston office of Fulbright & Jaworski LLP, where he specialized in antitrust and complex federal litigation. Mr. Curtis graduated from the Duke University School of Law in 1995. Mr. Curtis received his B.A. in Philosophy from Trinity University and his Doctor of Philosophy (D. Phil) from the University of Oxford (England).

Doug W. Jackson has served as vice president--marketing of Z-Tel since June 1999. From 1996 through 1999 he held the position of senior brand manager for the Coca-Cola Company and prior to that from 1992 to 1996 he was an associate product manager for Kraft General Foods Corp. Mr. Jackson received his B.A. from University of Virginia and his M.B.A. from University of Michigan.

Eduard J. Mayer has been a director of Z-Tel since July 1998 and vice president--strategic alliances since July 1999. Mr. Mayer is the president of Acorn Ventures, Inc., a venture investment company. Mr. Mayer holds a Bachelor of Commerce from the University of Windsor and a M.B.A. from New York University.

Douglas C. Williamson has been a director of Z-Tel since December 1998. Mr. Williamson has been senior vice president and managing director of Bank of America Capital Investors (formerly NationsBank Capital Corporation) since 1989. He is a member of the board of directors of CallWare Technologies, Inc., Empirical Software, Inc., GX Technology Corporation, HAHT Software, Inc., Med Solutions, Inc., Memorial Operations Company, North American Technologies Group, Inc. and Takeout Taxi Holdings, Inc. Mr. Williamson received a B.A. from Denison University and a M.B.A. from Columbia University.

Jeffrey A. Bowden, a founder of Z-Tel, has served as a director of Z-Tel since July 1998. Mr. Bowden is currently a director of the Boston Consulting Group. Mr. Bowden was vice president of Bell Atlantic Corporation from 1997 to 1998. Mr. Bowden was a vice president of The Nynex Corporation from 1994 to 1997 and vice president and a director of The Boston Consulting Group from 1988 to 1994. Mr. Bowden received his B.S. from the University of Michigan and his M.B.A. from the Harvard Graduate School of Business.

Buford H. Ortale has been a director of Z-Tel since July 1998. Since 1996 Mr. Ortale has been the president of Sewanee Ventures, LLC, a private investment firm. From 1993 to 1996 Mr. Ortale was a director and then a managing director of NationsBanc Capital Markets Inc. He is a member of the board of directors of Digital Medical Systems. Mr. Ortale received his B.A. degree from The University of the South and a M.B.A. from Vanderbilt University.

Laurence S. Grafstein has been a director of Z-Tel since October 1999. Mr. Grafstein is a co-founder of Gramercy Communications Partners, a private equity fund based in New York specializing in telecommunications investments. Previously, he was head of the global telecommunications practice at Credit Suisse First Boston. He is currently a member of the

<PAGE>

Executive Committee of the Wall Street Division of the United Jewish Appeal and a member of the boards of the Arts Connection and the Jerusalem Foundation. Mr. Grafstein received his B.A. from Harvard University, his M. Phil from Balliol College of Oxford University and an LL.B from the University of Toronto Law.

SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

All Section 16(a) filing requirements have been complied with since our initial public offering on December 14, 1999, except that for each of the following directors and officers, one form was not timely filed relating to the indicated number of transactions: Messrs. Bowden, Ortale, Grafstein, and Williamson, one transaction; Mr. Garrett, two transactions and his initial report upon becoming a Section 16(a) reporting person. In addition, the initial beneficial ownership report of Mr. Curtis did not accurately reflect the character of certain of his holdings.

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ITEM 11. EXECUTIVE COMPENSATION

SUMMARY COMPENSATION TABLE

The following table provides summary information concerning compensation paid or accrued by us to, or on behalf of, our "Named Executive Officers," which are (1) our Chief Executive Officer, (2) our four most highly compensated executive officers serving as executive officers at December 31, 1999 and (3) one additional individual who was an executive officer during 1999 but was not serving in that capacity on December 31, 1999. The aggregate amount of perquisites and other personal benefits, securities or property received by each of the Named Executive Officers was less than either \$50,000 or 10% of the total annual salary and bonus reported for that Named Executive Officer:

<TABLE>

<CAPTION>

NAME AND PRINCIPAL POSITION	ANNUAL COMPENSATION		LONG TERM COMPENSATION AWARDS	
	SALARY (\$)	BONUS (\$)	SHARES UNDERLYING OPTIONS	ALL OTHER COMPENSATION (\$)
<S>	<C>	<C>	<C>	
D. Gregory Smith President, Chief Executive Officer and Chairman	162,000	---	1,100	--
Russell T. Alba (1) Senior Vice President--Business Development and Chief Legal Officer	131,625	---	--	40,500
James A. Kitchen Senior Vice President--Chief Architect	162,000	---	27,500	--
J. Bryan Bunting Senior Vice President--Engineering and Technical Services	162,000	---	27,500	--
Charles W. McDonough Senior Vice President--Chief Technology Officer	162,000	---	27,500	--
David J. Malfara, Sr. President--Z-Tel Network Services, Inc.	137,500	---	357,500	12,000 (2)

</TABLE>

(1) Effective September 1999, Mr. Alba was no longer employed by us. "All Other Compensation" for Mr. Alba reflects amounts paid to him pursuant to a severance agreement.

(2) Represents compensation for consulting services provided by Malfara Associates, an assumed name of Mr. Malfara.

OPTION GRANTS IN LAST FISCAL YEAR

The following table contains information concerning the stock option grants made to each of the Named Executive Officers during the fiscal year ended December 31, 1999, subject to the following:

Under our 1998 Equity Participation Plan, stock options are generally granted as of the employee's start date. The options generally vest over a three year period commencing on the start date and expire ten years thereafter (unless the employee at the time of grant owned more

<PAGE>

than 10% of the total combined voting power of all classes of stock, in which case they expire over five years).

The 5% and 10% assumed annual rates of compounded stock price appreciation are mandated by the rules of the Securities and Exchange Commission. We cannot be certain that the actual stock price appreciation over the ten-year option term will be at the assumed 5% and 10% levels or at any other defined level. Unless the market price of the common stock appreciates over the option term, no value will be realized from the option grants. The potential realizable value is calculated by assuming that the fair market value of the common stock as determined by the Board of Directors on the date of grant of the options appreciates at the indicated rate of the entire term of the option and that the option is exercised at the exercise price and sold on the last day at the appreciated price.

<TABLE>

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INDIVIDUAL GRANTS

NAME	NUMBER OF SHARES OF COMMON STOCK UNDERLYING OPTIONS GRANTED	% OF TOTAL OPTIONS GRANTED TO EMPLOYEES IN 1999	WEIGHTED AVERAGE EXERCISE PRICE (\$/SH)	EXPIRATION DATE	POTENTIAL REALIZABLE VALUE AT ASSUMED ANNUAL RATES OF STOCK PRICE APPRECIATION FOR OPTION TERM	
					(5%) (\$)	10% (\$)
<S>	<C>	<C>	<C>	<C>	<C>	<C>
D. Gregory Smith	1,100	<1%	3.64	08/01/04	1,106	2,444
*Russell T. Alba	--	--	--	--	--	--
James A. Kitchen	27,500	<1%	5.45	10/09/09	94,256	238,862
J. Bryan Bunting	27,500	<1%	5.45	10/09/09	94,256	238,862
Charles W. McDonough	27,500	<1%	5.45	10/09/09	94,256	238,862
David J. Malfara, Sr.	40,700	<1%	3.64	01/26/09	93,169	236,110
	103,400	3%	3.64	02/01/09	236,701	599,846
	185,900	5%	3.64	07/26/09	425,558	1,078,447
	27,500	<1%	5.45	10/09/09	94,256	238,862

</TABLE>

* Effective September 1999, Mr. Alba was no longer employed by us.

<PAGE>

AGGREGATED OPTION EXERCISES IN LAST FISCAL YEAR AND YEAR-END OPTION VALUE TABLE

The following table shows information concerning stock option exercises during 1999 and stock option values as of the year ending December 31, 1999 by each of the Named Executive Officers. The value of unexercised in-the-money options is determined by subtracting the exercise price from the fair market value of the common stock based on \$40.375, the closing price of Z-Tel common stock as of December 31, 1999, multiplied by the number of shares underlying the options.

<TABLE>

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NAME	SHARES ACQUIRED ON EXERCISE (#)	VALUE REALIZED (\$)	NUMBER OF SECURITIES UNDERLYING UNEXERCISED OPTIONS AT FISCAL YEAR-END (#)		VALUE OF UNEXERCISED IN-THE MONEY OPTIONS AT FISCAL YEAR- END (\$)	
			EXERCISABLE	UNEXERCISABLE	EXERCISABLE	UNEXERCISABLE
<S>	<C>	<C>	<C>	<C>	<C>	<C>
D. Gregory Smith	--	--	336,111	214,989	12,347,042	\$7,897,617
*Russell T. Alba	--	--	129,800	--	4,768,203	0
James A. Kitchen	--	--	351,389	226,111	12,908,271	8,256,416
J. Bryan Bunting	10,000	133,600	119,861	172,639	4,403,098	6,292,115
Charles W. McDonough	197,490	3,008,951	0	270,010	0	10,323,557
David J. Malfara, Sr.	--	--	0	357,500	0	13,082,988

</TABLE>

* Effective September 1999, Mr. Alba was no longer employed by us.

COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION

The compensation committee of the Board of Directors consisted of Messrs. Ortale and Williamson during the year ended December 31, 1999, both of whom are non-employee directors. The compensation committee is responsible for all decisions concerning executive officer compensation, including decisions regarding grants of incentive stock options.

DIRECTOR COMPENSATION

Directors do not currently receive any cash compensation for services rendered to Z-Tel in their capacities as directors. Pursuant to the terms of The 1998 Equity Participation Plan of Z-Tel Technologies, Inc., each outside director who served as such as of the date of Z-Tel's initial public offering received options to purchase 1,100 shares of Z-Tel's common stock, and will receive options to purchase an additional 1,100 shares of Z-Tel's common stock on the date of each annual meeting of shareholders following such initial public offering.

<PAGE>

EXECUTIVE EMPLOYMENT AGREEMENTS, TERMINATION OF EMPLOYMENT AND
CHANGE-IN-CONTROL ARRANGEMENTS

We have entered into the following employment agreements:

<TABLE>

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OFFICER	TERM	ANNUAL SALARY	POSITION
<S>	<C>	<C>	<C>
D. Gregory Smith	July 1998 - July 2001	\$162,000	President, Chief Executive Officer and Chairman
Charles W. McDonough	August 1998 - August 2001	\$162,000	Senior Vice President - Chief Technology Officer
J. Bryan Bunting	August 1998 - August 2001	\$162,000	Senior Vice President - Engineering and Technical Services
James A. Kitchen	July 1998 - July 2001	\$162,000	Senior Vice President - Chief Architect

</TABLE>

The employment agreements with Messrs. Smith, McDonough, Bunting and
Kitchen also provide for:

- o automatic renewal for subsequent one year terms unless either party elects
not to renew prior to 90 days from the end of the then current term of the
agreement;
- o a bonus or other incentive compensation in an amount to be determined by
our compensation committee;
- o the payment of his base salary and any other benefits to which he would
have been entitled for the term of the agreement if he is terminated
without cause (as defined in the agreements);
- o generally, if a change of control occurs, the payment of two and
nine-tenths (2.9) times his base salary and any incentive or bonus paid in
the prior year if, within three years of the occurrence of a change of
control, specified events occur;
- o his obligation to keep our nonpublic information confidential; and
- o his obligation not to compete with us in the United States and not to
solicit our employees.

SEVERANCE AGREEMENT

We and Mr. Russell T. Alba are parties to an agreement, dated September
3, 1999, where we, among other things, agreed to pay a total severance amount of
\$324,000, which amount is payable monthly for a period of two years, provide
health benefits and provide for the extension of the exercise period of stock
options for Mr. Alba. Mr. Alba and we also provided each other with a mutual
release of any prior legal claims.

<PAGE>

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

The following table sets forth, as of March 24, 2000 (unless otherwise stated), the number of shares of our common stock beneficially owned by:

- o each person who we know to be a beneficial owner of 5% or more of our outstanding common stock;
- o each of our directors;
- o each of our Named Executive Officers; and
- o all executive officers and directors as a group.

<TABLE>
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BENEFICIAL OWNER	AMOUNT AND NATURE OF BENEFICIAL OWNERSHIP	PERCENT OF CLASS (1)
<S>	<C>	<C>
D. Gregory Smith (2)(3)	7,743,022	23.90
Carol Jane Smith (2)(3)	7,743,022	23.90
G/CJ Investments, L.P. (3)	5,500,000	17.18
Russell T. Alba (2)(4)	425,425	1.32
David J. Malfara, Sr. (2)(5)	60,042	*
James A. Kitchen (2)(6)	1,803,278	5.56
Charles W. McDonough (2)(7)	806,667	2.52
J. Bryan Bunting (2)(8)	380,417	1.18
Eduard J. Mayer (2)(9)	-0-	*
Buford H. Ortale (2)(10)	1,829,061	5.71
Douglas C. Williamson (2)(11)	-0-	*
Jeffrey Bowden (2)(12)	339,167	1.05
Laurence S. Grafstein (13)	-0-	*
Fulmead Ventures Limited (14)	2,348,520	7.34
BA Capital Company, L.P. (15)	1,780,325	5.56
Gramercy Z-Tel, L.P. (16)	3,074,280	9.61
All directors and officers as a group (18 persons)	13,599,079	40.57

</TABLE>

* Less than 1%.

(1) Beneficial ownership is determined in accordance with the rules of the Securities and Exchange Commission. In computing the aggregate number of shares beneficially owned by the individual stockholders and groups of stockholders described above and the percentage ownership of such individuals and groups, shares of common stock subject to options or warrants that are currently exercisable or exercisable within 60 days of the date of this report are deemed outstanding. Such shares, however, are not deemed outstanding for the purposes of computing the percentage ownership of the other stockholders or groups of stockholders.

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(2) The address for each of Messrs. Smith, Alba, Malfara, Kitchen, McDonough, Bunting, Mayer, Ortale, Williamson and Bowden and Mrs. Smith is c/o Z-Tel Technologies, Inc., 601 South Harbour Island Boulevard, Suite 220, Tampa, Florida 33602.

(3) D. Gregory Smith and Carol Jane Smith are husband and wife. The number of shares shown for D. Gregory Smith and for Carol Jane Smith each includes all of the shares held by G/CJ Investments, L.P., a Delaware limited partnership. G/CJ Investments, Inc., a Delaware corporation established and controlled by Mr. and Mrs. Smith, is the sole general partner of G/CJ Investments, L.P. The share amount also includes 397,222 shares for Mr. Smith and Mrs. Smith which are deemed to be beneficially owned by them by virtue of certain stock options that are currently exercisable or become exercisable within 60 days. The address of G/CJ Investments, L.P. is 300 Delaware Avenue, Suite 900, Wilmington, DE 19801.

(4) Includes 129,800 shares deemed to be beneficially owned by Mr. Alba by virtue of certain stock options that are currently exercisable or which become exercisable within 60 days. Effective September 1999, Mr. Alba was no longer employed by us.

(5) Includes 60,042 shares deemed to be beneficially owned by Mr. Malfara by virtue of certain stock options that are currently exercisable or which become exercisable within 60 days.

(6) Includes 427,778 shares deemed to be beneficially owned by Mr. Kitchen by virtue of certain stock options that are currently exercisable or which become exercisable within 60 days.

(7) Includes 59,177 shares deemed to be beneficially owned by Mr. McDonough by virtue of certain stock options that are currently exercisable or which become exercisable within 60 days.

(8) Includes 150,417 shares deemed to be beneficially owned by Mr. Bunting by virtue of certain stock options that are currently exercisable or which become exercisable within 60 days.

(9) Does not include 2,348,520 shares owned directly by Fulmead Ventures Limited, which is beneficially owned by The Mayer Trust. Mr. Mayer is a principal beneficiary of The Mayer Trust. Mr. Mayer disclaims beneficial ownership of these shares as he does not have voting or dispositive power with respect to these shares.

(10) Includes 158,036 shares held by a general partnership with which Mr. Ortale is affiliated and 68,622 shares held by a trust of which Mr. Ortale is a trustee.

(11) Excludes 1,780,325 shares owned by BA Capital Company, L.P., of which Mr. Williamson is a senior officer. Mr. Williamson disclaims beneficial ownership of the shares owned by BA Capital Company, L.P.

(12) Includes 229,167 shares deemed to be beneficially owned by Mr. Bowden by virtue of certain stock options that are currently exercisable or which become exercisable within 60 days.

(13) Excludes 3,074,280 shares owned by Gramercy Z-Tel L.P., of which Mr. Grafstein is a senior officer. Mr. Grafstein disclaims beneficial ownership of the shares owned by Gramercy Z-Tel L.P.

(14) This information is derived from a Schedule 13G dated February 4, 2000 filed jointly by The Mayer Trust, Eduard J. Mayer, Mutual Risk Management Ltd., Mutual Risk Management (Holdings) Limited, Hemisphere Trust (Jersey) Limited, Hemisphere Trustees Limited, Hemisphere Nominees Limited, Hemisphere Investments Limited, and Fulmead Ventures Limited. Each of these parties is shown to have shared voting and dispositive power with respect to all of the shares shown. Eduard J. Mayer disclaims beneficial ownership of the shares shown. The address of Fulmead Ventures Limited is Akara Bldg., 24 Castro Street, Wickhams Cay I, Road Town, Tortola, British Virgin Islands.

(15) This information is derived from a Schedule 13G dated February 14, 2000 filed jointly by BA Capital Company, L.P., BA SBIC Management, LLC, BA Equity Management, L.P., BA Equity Management GP, LLC, Walter W. Walker, Jr., and Bank of America Corporation. Each of these parties is shown to have sole voting and

<PAGE>

dispositive power with respect to all of the shares shown. The address of BA Capital Company, L.P., is 901 Main Street, 22nd Floor, Dallas, TX 75202-3714.

(16) This information is derived from a Schedule 13G filed February 14, 2000 and dated February 2000 filed jointly by Gramercy Z-Tel L.P., Gramercy Z-Tel LLC and Communicapital Partners (Cayman), L.P. Each of these parties is shown to have shared voting and dispositive power with respect to all of the shares shown. The address of Gramercy Z-Tel L.P. is 712 Fifth Avenue, New York, NY 10019.

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ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

PURCHASES OF COMMON STOCK

On January 15, 1998, Rob Curtis purchased 110,000 shares of our common stock for a purchase price of \$125,000. Mr. Curtis' note to us in the principal amount of \$93,750, bears interest at a rate of 8% per annum, matures on December 31, 2001 and is secured by a pledge of his common stock. The largest amount of indebtedness under the note during 1999 was \$93,750, and the outstanding balance as of March 23, 2000 was \$0.

In agreements dated September 1, 1998, each of D. Gregory Smith, James A. Kitchen, Charles W. McDonough and J. Bryan Bunting, together referred to as the officer investors, purchased, in the aggregate, 9,570,000 shares of our common stock for an aggregate purchase price of \$10.88 million. In connection with the purchase of these shares, we loaned: (1) \$750,000 to Mr. Smith for the purchase price of 660,000 of his shares, (2) \$750,000 to Mr. Kitchen for the purchase price of 660,000 of his shares; (3) \$468,750 to Mr. McDonough for the purchase price of 550,000 of his shares and (4) \$187,500 to Mr. Bunting for the purchase price of 220,000 of his shares. These loans, which bear interest at an 8% annual rate and mature on December 31, 2001, are secured by a pledge to us of the common stock. The largest amount of indebtedness under the notes during 1999 was \$750,000, \$750,000, \$468,750, and \$187,500, respectively, and the outstanding note balances as of March 23, 2000 were \$0, \$500,000, \$468,750 and \$187,500, respectively.

These agreements permit Messrs. Smith and Kitchen, first, and us, second, to purchase from the officer investors a portion of their shares in the event of a termination (as defined in the agreements) of the officer's employment with us. This purchase option must be exercised within 30 days after the termination of the respective officer's employment with us. In addition, the purchase option lapses automatically if we are involved in a corporate transaction (as defined in the agreements).

After March 1, 2000, the officer investors have a right, subject to quantity limitations we determine, or determined by underwriters, if applicable, to request that we register their common stock that is no longer subject to the purchase option.

On September 1, 1999, Mr. Smith purchased an additional 85,800 shares of our common stock for \$97,500 as a result of his exercise of his purchase option to buy shares from an individual who left the company. Mr. Smith paid for this purchase with a note under which the largest amount of indebtedness during 1999 was \$97,500. The principal balance of the note on March 23, 2000 was \$0, and was on substantially the same terms as Mr. Smith's other note to the company.

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PURCHASE OF SERIES B PREFERRED STOCK

On September 22, 1999, we sold an additional 2,964,500 shares of Series B Preferred Stock for an aggregate consideration of approximately \$10 million. Included in that offering were 148,519 shares purchased for \$3.37 per share by Fulmead Ventures Limited, which is beneficially owned by a trust of which Eduard J. Mayer is a beneficiary, and 148,267 shares purchased for \$3.37 per share by Buford H. Ortale.

PURCHASE OF SERIES C PREFERRED STOCK

On October 8, 1999, Gramercy Z-Tel L.P. purchased 3,074,280 shares of Series C Preferred Stock for a purchase price of \$15 million.

STOCK PURCHASE AGREEMENT AND STOCKHOLDERS' AGREEMENT

REGISTRATION RIGHTS. The terms of the Series A Preferred Stock and Series C Preferred Stock provide that the holders of common stock issued upon conversion of, or as a dividend on, Series A Preferred Stock or Series C Preferred Stock, as the case may be, may require us to register that common stock under the Securities Act beginning no earlier than 180 days after the effective date of a registration statement for an initial public offering of our common stock. Holders of common stock issued upon conversion of, or as a dividend on, Series A Preferred Stock and Series C Preferred Stock also have the right to cause us to register that common stock on Form S-3 when it becomes available to us if they propose to register securities having a value of at least \$10 million. We will bear all registration expenses incurred in connection with the first three of these demands for registration. In addition, if we propose to register securities under the Securities Act, other than registrations on Form S-4 or Form S-8, then, the holders of common stock issued upon conversion of, or as a dividend on, Series A Preferred Stock, Series B Preferred Stock or Series C Preferred Stock have a right, subject to quantity limitations determined by underwriters if the offering involves an underwriting, to request that we register such holders' common stock. If holders of common stock issued upon conversion of, or as a dividend on, Series A Preferred Stock, Series B Preferred Stock or Series C Preferred Stock participate in that registration, holders of common stock issued upon conversion of, or as a dividend on, Series A Preferred Stock and Series C Preferred Stock will have priority over all other holders of common stock (other than Z-Tel).

TRANSACTIONS WITH OLYMPUS MANAGEMENT GROUP, INC.

Since January 1, 2000, Z-Tel Communications, Inc., one of our wholly owned subsidiaries, has sub-sub leased, on a month-to-month basis, two pieces of real property from Olympus Management Group, Inc., an entity of which Mr. Smith is a 100% shareholder. The rental obligation under these sub-sub leases is \$6,800 per month. The sub-sub leases are terminable by either party at any time.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON
FORM 8-K

- (a) 1. The following financial statements of Z-Tel Technologies, Inc. and the report thereon of PricewaterhouseCoopers LLP dated February 15, 2000 are filed as part of this report:
- Report of Independent Certified Public Accountants.
 - Consolidated Balance Sheets, December 31, 1999 and December 31, 1998.
 - Consolidated Statements of Operations for the year ended December 31, 1999 and the period from January 15, 1998 (Inception) through December 31, 1998.
 - Consolidated Statement of Changes in Stockholders' Equity (Deficit) for the year ended December 31, 1999 and the period from January 15, 1998 (Inception) through December 31, 1998.
 - Consolidated Statements of Cash Flows for the year ended December 31, 1999 and the period from January 15, 1998 (Inception) through December 31, 1998.
 - Notes to Financial Statements.
2. The following Financial Statement Schedules are included herein:
- Schedules are not submitted because they are not applicable or not required or because the required information is included in the financial statements or the notes thereto.
3. The following exhibits are filed as part of this report (exhibits marked with an asterisk have been previously filed with the Commission as indicated, as a correspondingly numbered Exhibit to Z-Tel Registration Statement on Form S-1 (Commission File No. 333-89063) originally filed on October 14, 1999, as subsequently amended, and are incorporated herein by this reference):
- 3.1* Amended and Restated Certificate of Incorporation of Z-Tel
 - 3.2* Amended and Restated Bylaws of Z-Tel
 - 4.1* Form of Common Stock Certificate

- 4.2 See Exhibits 3.1 and 3.2 of this Registration Statement for provisions of the Amended and Restated Certificate of Incorporation and the Bylaws of Z-Tel defining rights of security holders
- 10.1.1* Stockholders' Agreement dated October 8, 1999, between and among the company, BA Capital Corporation, Sewanee Partners II, L.P., Gramercy Z-Tel LLC and the other parties set forth therein
- 10.1.2* Employment Agreement dated July 1998 between the Company and D. Gregory Smith
- 10.1.3* Employment Agreement dated September 1999 between the Company and John Hutchens
- 10.1.4* Employment Agreement dated August 1998 between the Company and Charles W. McDonough
- 10.1.5* Employment Agreement dated August 1998 between the Company and J. Bryan Bunting
- 10.1.6* Employment Agreement dated July 1998 between the Company and James A. Kitchen
- 10.1.7* Investment Agreement dated March 15, 1999 between the Company and CMB Capital LLC
- 10.2* 1998 Equity Participation Plan
- 21* List of subsidiaries
- 27 Financial Data Schedules

(b) The Company did not file any reports on Form 8-K during the year ended December 31, 1999.

<PAGE>

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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, as of the 23rd day of March, 2000.

Z-TEL TECHNOLOGIES, INC.

By: /s/ D. GREGORY SMITH

D. Gregory Smith, President and
Chief Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant in the capacities and on the dates indicated.

SIGNATURE -----	TITLE -----	DATE ----
/s/ D. GREGORY SMITH ----- D. Gregory Smith	President, CEO, Chairman of the Board and Director (Principal Executive Officer)	March 23, 2000
/s/ JOHN M. HUTCHENS ----- John M. Hutchens	Chief Financial Officer (Principal Financial and Accounting Officer)	March 23, 2000
/s/ DOUGLAS C. WILLIAMSON ----- Douglas C. Williamson	Director	March 23, 2000
/s/ JEFFREY A. BOWDEN ----- Jeffrey A. Bowden	Director	March 23, 2000
/s/ EDUARD J. MAYER ----- Eduard J. Mayer	Director	March 23, 2000
/s/ BUFORD H. ORTALE ----- Buford H. Ortale	Director	March 23, 2000

<PAGE>

/S/ LAURENCE S. GRAFSTEIN Director

March 23, 2000

Laurence S. Grafstein

EXHIBIT LIST

(Exhibits marked with an asterisk have been previously filed with the Commission as indicated and are incorporated herein by this reference)

- 3.1* Amended and Restated Certificate of Incorporation of Z-Tel
- 3.2* Amended and Restated Bylaws of Z-Tel
- 4.1* Form of Common Stock Certificate
- 4.2 See Exhibits 3.1 and 3.2 of this Registration Statement for provisions of the Amended and Restated Certificate of Incorporation and the Bylaws of Z-Tel defining rights of security holders
- 10.1.1* Stockholders' Agreement dated October 8, 1999, between and among the company, BA Capital Corporation, Sewanee Partners II, L.P., Gramercy Z-Tel LLC and the other parties set forth therein
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- 10.2* 1998 Equity Participation Plan
- 21* List of subsidiaries
- 27 Financial Data Schedules

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SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 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 JUNE 30, 2000

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

For the Transition Period From _____ to _____

Commission File Number 000-28467

Z-TEL TECHNOLOGIES, INC.

(Exact Name of Registrant as Specified in its Charter)

Delaware

59-3501119

(State of Other Jurisdiction of
Incorporation or Organization)

(I.R.S. Employer
Identification Number)

601 South Harbour Island Boulevard, Suite 220
Tampa, Florida 33602

(Address of Principal Executive Offices)

(813) 273-6261

(Registrant's Telephone Number, Including Area Code)

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

At August 9, 2000 the Registrant had outstanding 33,495,147 shares of \$.01 par value common stock.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (IN THOUSANDS, EXCEPT SHARE DATA)

JUNE 30, DECEMBER 31,

	2000	1999
	-----	-----
ASSETS		
Current assets:	(Unaudited)	
Cash and cash equivalents	\$ 10,656	\$ 101,657
Accounts receivable, net of allowance for doubtful accounts of approximately \$3,451 at June 30, 2000 and \$408 at December 31, 1999	36,476	4,245
Prepaid expenses and other current assets	5,074	2,304
Total current assets	52,206	108,206
Property and equipment, net	52,018	28,549
Investments	7,088	--
Intangible assets, net	65,918	--
Other	3,220	922
Total assets	\$ 180,450	\$ 137,677
	=====	=====
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 34,586	\$ 9,165
Current portion of long-term debt and capital lease obligations	4,835	3,726
Total current liabilities	39,421	12,891
Long-term debt and capital lease obligations	17,216	10,408
Total liabilities	56,637	23,299
	-----	-----
Commitments and contingencies (Notes 4 and 6)		
Stockholders' equity:		
Common stock, \$.01 par value; 150,000,000 shares authorized; 33,681,175 and 32,159,911 shares issued; 33,401,497 and 31,880,236 outstanding, respectively	337	322
Notes receivable from stockholders	(539)	(1,683)
Unearned stock compensation	(494)	(2,487)
Additional paid-in capital	206,414	167,637
Accumulated deficit	(87,624)	(49,093)
Accumulated other comprehensive income	6,037	--
Treasury stock, 279,675 shares at cost	(318)	(318)
Total stockholders' equity	123,813	114,378
	-----	-----
Total liabilities and stockholders' equity	\$ 180,450	\$ 137,677
	=====	=====

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)
(UNAUDITED)

THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
-----	-----	-----	-----
2000	1999	2000	1999
-----	-----	-----	-----

Revenues	\$ 40,157	\$ 761	\$ 54,133	\$ 1,425
Operating expenses:				
Network operations	25,137	978	34,967	1,792
Sales and marketing	10,635	666	17,454	1,848
Research and development	1,790	352	3,089	1,465
General and administrative	20,878	2,390	31,339	4,987
Depreciation and amortization	4,404	863	6,492	1,664
Total operating expenses	62,844	5,249	93,341	11,756
Operating loss	(22,687)	(4,488)	(39,208)	(10,331)
Nonoperating income (expense):				
Interest income	455	114	1,741	232
Interest expense	(823)	(1,237)	(1,064)	(1,451)
Total nonoperating income (expense)	(368)	(1,123)	677	(1,219)
Net loss	(23,055)	(5,611)	(38,531)	(11,550)
Less mandatorily convertible redeemable preferred stock dividends		(414)		(606)
Net loss attributable to common stockholders	\$ (23,055)	\$ (6,025)	\$ (38,531)	\$ (12,156)
Weighted average common shares outstanding	33,042,008	14,411,100	32,499,640	14,411,100
Basic and diluted net loss per share	\$ (0.70)	\$ (0.42)	\$ (1.19)	\$ (0.84)

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
(IN THOUSANDS, EXCEPT FOR SHARE DATA)
(UNAUDITED)

	COMMON STOCK		NOTES RECEIVABLE FROM STOCKHOLDERS	UNEARNED STOCK COMPENSATION	ADDITIONAL PAID-IN CAPITAL
	SHARES	PAR VALUE			
Balances, December 31, 1999	31,880,236	\$ 322	\$ (1,683)	\$ (2,487)	\$167,637
Issuance of common stock for acquisition of Touch 1	1,100,000	11			39,275
Issuance of common stock for exercise of stock options	421,261	4			1,314
Repayment of Stockholders' note			1,144		
Vesting of stock options granted below intrinsic value				1,993	(2,467)
Warrants extinguished with debt					655
Net Loss					
Foreign currency translation adjustment					
Unrealized Gain on Investments					
Comprehensive Income					
Balances, June 30, 2000	33,401,497	\$ 337	\$ (539)	\$ (494)	\$206,414

	ACCUMULATED	ACCUMULATED	TREASURY	TOTAL
	EQUITY	OTHER COMPREHENSIVE INCOME	STOCK	STOCKHOLDERS' EQUITY
Balances, December 31, 1999	\$ (49,093)	\$ --	\$ (318)	\$ 114,378
Issuance of common stock for acquisition of Touch 1				39,286
Issuance of common stock for exercise of stock options				1,318
Repayment of Stockholders' note				1,144
Vesting of stock options granted below intrinsic value				(474)
Warrants extinguished with debt				655

Net Loss	(38,531)			(38,531)
Foreign currency translation adjustment		(1)		(1)
Unrealized Gain on Investments		6,038		6,038
Comprehensive Income				(32,494)
Balances, June 30, 2000	\$ (87,624)	\$ 6,037	\$ (318)	\$ 123,813

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)
(UNAUDITED)

	Six Months Ended June 30	
	2000	1999
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$ (38,531)	\$ (11,551)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	6,492	1,664
Provision for bad debts	2,380	242
Change in operating assets and liabilities:		
Increase in accounts receivable	(25,762)	(671)
Increase in prepaid expenses and other current assets	(3,552)	(860)
Increase in accounts payable and accrued liabilities	13,363	49
Increase in deferred revenue	3,376	
Other	181	42
Total adjustments	(3,522)	466
Net cash used in operating activities	(42,053)	(11,085)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale and leaseback transaction		9,943
Purchases of property and equipment	(20,154)	(6,242)
Investment in securities available for sale	(1,050)	
Purchase of Touch 1, net of cash acquired	(8,955)	
Net cash provided by (used in) investing activities	(30,159)	3,701
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from exercise of stock options	1,317	
Proceeds from issuance of mandatorily convertible redeemable preferred stock		3,548
Proceeds from notes receivable	1,144	
Payments on long-term debt and capital lease obligations	(21,250)	(1,886)
Net cash provided by (used in) financing activities	(18,789)	1,662
Net decrease in cash and cash equivalents	(91,001)	(5,722)
Cash and cash equivalents, beginning of period	101,657	7,973
Cash and cash equivalents, end of period	\$ 10,656	\$ 2,251
NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Property and equipment acquired under capital lease obligations	\$ --	\$ 9,943
ACQUISITION OF TOUCH 1		
Fair value of assets acquired	\$ 85,967	\$ --
Liabilities assumed	(37,979)	--
Common stock issued	(40,201)	--
Net cash paid for acquisition	7,787	--
Cash acquired in acquisition	1,168	--

Cash paid for acquisition	-----	-----
	\$ 8,955	\$ --
	-----	-----

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE FINANCIAL STATEMENTS.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. NATURE OF BUSINESS

DESCRIPTION OF BUSINESS

Z-Tel Technologies, Inc. and subsidiaries ("Z-Tel" or the "Company") incorporated in Delaware on January 15, 1998 as Olympus Telecommunications Group, Inc. In March 1998, Olympus Telecommunications Group, Inc. changed its name to Z-Tel Technologies, Inc. Z-Tel Technologies, Inc. is the parent company, and has no other operations. The Company has eight wholly owned subsidiaries: Z-Tel Communications, Inc., Z-Tel Business Networks, Inc., Z-Tel Holdings, Inc., Z-Tel Communications of Virginia, Inc., Z-Tel, Inc., Z-Tel Network Services, Inc., Z-Tel Investments, Inc. and Touch 1 Communications, Inc.

Z-Tel is an emerging provider of advanced, integrated telecommunications services targeted to residential subscribers. Z-Tel offers local and long distance telephone services in combination with enhanced communication features accessible through the telephone or the Internet. Z-Tel offers its Z-Line Home Edition service in New York, Texas, Massachusetts, Pennsylvania, and Georgia. Z-Tel also provides long-distance services to customers nationally.

2. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared by the Company in accordance with generally accepted accounting principles for interim financial information and are in the form prescribed by the Securities and Exchange Commission in 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. The interim unaudited financial statements should be read in conjunction with the audited financial statements of the Company as of and for the year ended December 31, 1999, included in the Company's Annual Report on Form 10-K. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Operating results for the three and six months ended June 30, 2000 are not necessarily indicative of the results that may be expected for the year ending December 31, 2000.

Certain amounts in the prior period's consolidated financial statements have been reclassified to conform to the current period presentation.

PRINCIPLES OF CONSOLIDATION

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All material intercompany accounts and transactions have been eliminated.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (CONTINUED)

INVESTMENTS

Included in investments are available for sale securities and investments accounted for utilizing the cost method of accounting for those investments without a readily identifiable market. In accordance with Statement of Financial Accounting Standards Board No. 115, "Accounting for Certain Investments in Debt and Equity Securities," securities that are available for sale are reported at fair value. At June 30, 2000, the Company had approximately \$6.7 and \$0.4 million in available for sale securities and investments accounted for at cost, respectively. There was an increase of approximately \$6.0 million in fair value, using the specific identification method for calculating the unrealized gain, for the three months ended June 30, 2000 recorded as a separate component of comprehensive income in equity.

NEW ACCOUNTING PRONOUNCEMENTS

In December 1999, the SEC issued Staff Accounting Bulletin No. 101 ("SAB 101"), "Revenue Recognition in Financial Statements." While not intended to change current literature related to revenue recognition, SAB 101 provides additional guidance on revenue recognition policies and procedures. The Company believes that its current accounting policies and procedures related to revenue recognition comply with SAB 101.

3. ACQUISITION OF TOUCH 1

The Company completed the acquisition of Touch 1 Communications, Inc. ("Touch 1"), a reseller of long distance service to subscribers throughout the United States, on April 14, 2000. Touch 1 is the parent company to its two wholly owned subsidiaries, direcTel, Inc. and direcCONNECT, Inc. The purchase price for Touch 1 consisted of 1.1 million shares of the Company's common stock at a price of \$35.71 per share, approximately \$9.0 million in cash, and approximately \$1.0 million in transaction and related fees. The acquisition of Touch 1 was accounted for using the purchase method of accounting and, accordingly, the results of operation of Touch 1 for the period beginning April 10, 2000 (the closing date for accounting purposes) are included in the accompanying condensed consolidated financial statements. The acquisition of Touch 1 resulted in approximately \$67.0 million of intangible assets, preliminarily allocated to customer lists and goodwill, which are being amortized, on the straight line basis, over periods of five and twenty years, respectively.

The following unaudited pro forma information presents a summary of our consolidated results of operations as if the acquisition had occurred at the beginning of the periods presented.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (CONTINUED)

In thousands, except per share data	SIX MONTHS ENDED	
	June 30,	
	2000	1999
	----	----
Revenues	\$ 85,064	\$ 31,531
Net loss	(46,556)	(17,115)
Loss per share	(1.14)	(1.10)

The pro forma condensed consolidated financial information is not necessarily indicative of what Z-Tel's results of operations would have been had the acquisition been completed at the beginning of the period presented or the future results of the Company's operations.

4. COMMITMENTS AND CONTINGENCIES

The Company has disputed billings and access charges from certain inter-exchange carriers (IXCs) and incumbent local exchange carriers (ILECs). The Company contends these billings and access charges are not in accordance with the interconnection, service level, or tariff agreements entered between the Company and certain IXCs and ILECs. The Company has paid for a portion of these disputes and management believes that the Company will prevail in these disputes. At June 30, 2000 and December 31, 1999, the disputed amounts were approximately \$4.9 and \$2.3 million, respectively.

The Company has entered into an agreement with a service firm to provide various content and new service offerings through the telephone. Under this agreement Z-Tel has invested \$3.0 million and is committed to an additional \$4.0 million in cash payments for future services. This contract provides for early termination under certain circumstances with adjustments to the commitments.

5. COMPUTATION OF NET LOSS PER SHARE

Basic and diluted net loss per share are computed by dividing net loss attributable to common stockholders by the weighted average number of common shares outstanding during the period. Incremental shares of common stock equivalents are not included in the calculation of diluted net loss per share as the inclusion of such equivalents would be anti-dilutive.

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (CONTINUED)

Net loss per share is calculated as follows:

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2000	1999	2000	1999
(In thousands, except share and per share data)				
Basic and diluted net loss per share:				
Loss attributable to common stockholders:				
Net loss	\$ (23,055)	\$ (5,611)	\$ (38,531)	\$ (11,550)
Less mandatorily convertible redeemable preferred stock dividends	--	(414)	--	(606)
	-----	-----	-----	-----
Loss attributable to common stockholders	\$ (23,055)	\$ (6,025)	\$ (38,531)	\$ (12,156)
	=====	=====	=====	=====
Weighted average common shares outstanding	33,042,008	14,411,100	32,499,640	14,411,100
	=====	=====	=====	=====
Basic and diluted net loss per share	\$ (0.70)	\$ (0.42)	\$ (1.19)	\$ (0.84)
	=====	=====	=====	=====

For each of the periods presented, basic and diluted net loss per share are the same. Unexercised options to purchase 9,421,912 and 7,156,284 shares of common stock at June 30, 2000 and December 31, 1999, respectively, which could potentially dilute basic earnings per share in the future, were not included in the computation of diluted net loss per share for these periods because to do so would have been anti-dilutive in each case.

6. LEGAL AND REGULATORY PROCEEDINGS

On June 9, 2000, PTEK Holdings, Inc. and Premiere Communications, Inc.

(collectively, "PTEK") filed a lawsuit against the Company, Z-Tel Communications, Inc., David Gregory Smith, Z-Tel's Chairman, Chief Executive Officer and President, Eduard Mayer, one of Z-Tel's directors and James Kitchen, a Senior Vice President of Z-Tel. In the lawsuit, PTEK asserts claims for patent infringement, misappropriation of trade secrets, breach of contract, conversion, misappropriation of and conspiracy to misappropriate corporate opportunities and tortious interference with contractual relations between PTEK and its employees and with PTEK's actual and prospective business relationships. PTEK seeks preliminary and permanent injunctive relief against the defendants, an equitable trust of an unspecified amount of common stock of Z-Tel, return of proceeds, with interest, of moneys realized by Mr. Smith from the exercise and sale of PTEK options, disgorgement of economic benefits wrongfully obtained, an unspecified amount of actual and punitive damages arising out of the common law claims, treble damages for willful infringement of the PTEK patent and costs. The defendants believe the claims asserted in the lawsuit are without merit, intend to defend it vigorously and have asserted counterclaims against PTEK and Mr. Jones. It is the opinion of management that the lawsuit will be resolved without material adverse effect on the Company's financial position, results of operations, or cash flows.

In the ordinary course of business, the Company is involved in legal proceedings that are generally incidental to its operations. In addition, from time to time the Company is the

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Z-TEL TECHNOLOGIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (CONTINUED)

subject of customer complaints filed with the state utility commissions of the states in which it operates or the FCC. Most complaints are handled informally and at this time there are no formal proceedings pending. While there can be no assurance of the ultimate disposition of incidental legal proceedings or customer complaints, the Company does not believe their disposition will have a material adverse effect on the Company's consolidated results of operations or financial position.

7. SUBSEQUENT EVENTS

In July 2000, the Company filed a Certificate of Designation authorizing the issuance of 5.0 million shares of Series D convertible preferred stock ("Series D Preferred"). The Company has received commitments to purchase 4,688,247 shares of the Series D Preferred at a price of \$12.00 for aggregate proceeds of \$56.3 million, \$43.1 million of which have been received by the Company. The Series D Preferred is convertible at a conversion price of \$12.00, which price is subject to adjustment, into common stock at the option of the holder (i.e., initially convertible on a one-for-one basis); however, there are certain circumstances that provide for a forced conversion of the stock by the Company. The Series D Preferred is mandatorily redeemable 8 years from the original issue date, has an 8% cumulative dividend payable at times in cash and at times with in-kind contributions of additional Series D Preferred and has certain liquidation preferences and voting rights. Each purchaser of Series D Preferred received a warrant to purchase a number of shares of Z-Tel common stock equal to one-half of the amount of Series D Preferred purchased by each investor. Each warrant is exercisable at a price of \$13.80 per share subject to certain adjustments.

In July 2000, the Company entered into an accounts receivable facility with RFC Capital Corporation ("RFC") providing for the sale of certain of the Company's accounts receivable to RFC. RFC has agreed to purchase up to \$25 million of the Company's accounts receivable, \$10 million of which is subject to the Company's meeting certain conditions, with provisions for a

commitment of up to \$50 million, subject to successful syndication of the receivables sales program by RFC. The Company has not utilized any of this facility to date.

In August 2000, the Company entered into an agreement with a service firm to outsource customer provisioning through electronic bonding with incumbent local exchange carriers. Under this agreement, Z-Tel is committed to approximately \$0.5 million cash payment for set-up fees and minimum commitment fees for the next three years subject to the successful completion by the service firm of certain obligations in the future. The minimum commitments under the contract, subject to certain adjustments, are approximately \$4.0, \$7.0, and \$9.0 million over the next three years. This contract provides for various termination arrangements with related severance fees.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

This Management's Discussion and Analysis of Financial Condition and Results of

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Operations and other sections of this Quarterly Report on Form 10-Q contain forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those projected in the forward-looking statements as a result of certain factors. Factors that may affect our results of operations include, but are not limited to, our limited operating history and cumulative losses, uncertainty of customer demand, rapid expansion, potential software failures and errors, potential network and interconnection failure, dependence on local exchange carriers, dependence on third party vendors, dependence on key personnel, uncertainty of government regulation, legal and regulatory uncertainties, and competition. Specifically, Verizon Communications, Inc., a local exchange carrier on which we rely to accomplish certain steps in customer provisioning, service and billing for customers in certain locales in New York, Massachusetts and Pennsylvania, is experiencing a strike involving its principal labor force. We do not currently believe that the strike will significantly impact our operations in these states. We disclaim any obligation to update information contained in any forward-looking statement. In addition to the factors noted above, other risks, uncertainties, assumptions, and factors that could affect the Company's financial results are described in the Company's 1999 Annual Report on Form 10-K, filed with the Securities and Exchange Commission on March 28, 2000.

The forward-looking statements are based on the belief of our management, as well as assumptions made by and information currently available to our management. Forward-looking statements also may be included in other written and oral statements made or released by us. You can identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. The words "believe," "anticipate," "intend," "expect," "estimate," "project" and similar expressions are intended to identify forward-looking statements. Forward-looking statements describe our expectations today of what we believe is most likely to occur or reasonably achievable in the future, but they do not predict or assure any future occurrence and may turn out to be wrong.

We caution you not to place undue reliance on these forward-looking statements, which speak only as of the date of this document.

OVERVIEW

We are an emerging provider of advanced, integrated telecommunications services targeted primarily to residential subscribers. For management purposes, we are organized into one reportable operating segment. We offer local and long distance telephone services in combination with enhanced communication features accessible through the telephone or the Internet. The nature of our business is

rapidly evolving and we have a limited operating history. As a result, we believe that period-to-period comparisons of our revenues and operating results, including our network operations and other operating expenses as a percentage of total revenue, are not meaningful and should not be relied upon as indicators of future performance. We do not believe that our historical growth rates are indicative of future results.

Z-Line Home Edition is our principal service offering. Z-Line Home Edition includes low-priced local and long-distance (1+) residential telephone services using a customer's existing telephone number, bundled with enhanced features, including caller identification, call forwarding, three-way calling, speed dialing, and dial-up remote access through our Z-Line Anywhere access card product, the full functionality of the Personal Communication Center ("PCC") and, for an additional fee, Internet access. We offer Z-Line Home Edition service in New York, Texas, Massachusetts and Pennsylvania, and began offering service in Georgia during July 2000. We anticipate entering additional states before the end of the third quarter of 2000.

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We began offering an access card service, similar to our current Z-Line Anywhere service, in the quarter ended December 31, 1998. Z-Line Anywhere is our access card product that allows a customer to make long-distance calls using Z-Tel's network from any phone simply by dialing a local access or toll-free 1-800 number. No change in phone service is required. Subscribers of Z-Line Anywhere also receive the full functionality of our PCC. Z-Line Anywhere is offered nationwide. Z-Line Anywhere customers are billed monthly in arrears, and the associated revenue is recognized in the month of service.

We completed the acquisition of Touch 1 Communications, Inc. ("Touch 1"), on April 14, 2000, with a closing date of April 10, 2000 for accounting purposes. The purchase price of Touch 1 consisted of 1.1 million shares of our common stock and \$9.0 million in cash. Touch 1 provides employees in sales, provisioning, and customer service. We anticipate that this acquisition will provide operating efficiencies and lower customer acquisition costs. We believe that Touch 1 also has provided us with the opportunity to further grow our back-office operations to provide capacity for market entry into new states.

We used the purchase accounting method for our acquisition of Touch 1. Therefore, in accordance with the purchase accounting method, the below discussions of the results of operations and liquidity and capital resources do not include any discussions regarding Touch 1 prior to our acquisition of Touch 1 on April 10, 2000. This treatment is in accordance with the adoption of the purchase method of accounting. A pro forma discussion and schedule is included in Footnote 3 to the financial statements that display the pro forma statement of operations of us and Touch 1 for the six months ended June 30, 2000.

RESULTS OF OPERATIONS

REVENUE. Revenue increased by \$39.4 million to \$40.2 million for the three months ended June 30, 2000, compared to \$0.8 million for the same period in the prior year. The increase in revenue is primarily the result of the average Home Edition customer count of 129,000 for the three months ended June 30, 2000, compared to 0 for the same period in the prior year. The purchase of Touch 1 in the second quarter of 2000 provided an increase in revenue of \$12.0 million from its existing 1+ long-distance offering for the three months ended June 30, 2000 and 1999.

Revenue increased by \$52.7 million to \$54.1 million for the six months ended June 30, 2000, compared to \$1.4 million for the same period in the prior year. The increase in revenue is primarily the result of the average Home Edition customer count of 105,000 for the six months ended June 30, 2000, compared to 0 for the same period in the prior year. The revenue from Touch 1 contributed \$12.0 million to the increase. The following tables outline the approximate number of subscribers for Z-Line Home Edition, Z-Line Anywhere and Touch 1 (1+) long distance services as of the end of the period:

TYPE OF SERVICE	June 30, 2000	June 30, 1999
Z-Line Home Edition Subscribers	170,000	0
Z-Line Anywhere and Touch 1 (1+)		
	13	
14		
Long Distance Services Subscribers	301,500	80,000

NETWORK OPERATIONS. Network operations expense increased by \$24.1 million to \$25.1 million for the three months ended June 30, 2000, compared to \$1.0 million for the same period in the prior year. Network operations expense increased by \$33.2 million to \$35.0 million for the six months ended June 30, 2000, compared to \$1.8 million for the same period in the prior year. The network operations expense primarily consists of fixed and variable transmission expenses for interconnection agreements with incumbent local exchange carriers (ILECs), service level agreements with inter-exchange carriers (IXCs), and transmission services based on tariff arrangements. The increase in network operation expense in both the three months and six months ended June 30, 2000 is the result of our subscriber growth.

SALES AND MARKETING. Sales and marketing expense increased \$9.9 million to \$10.6 million for the three months ended June 30, 2000, compared to \$0.7 million for the same period in the prior year. Sales and marketing expense increased \$15.7 million to \$17.5 million for the six months ended June 30, 2000, compared to \$1.8 million for the same period in the prior year. The sales and marketing expense primarily consists of telemarketing, direct mail, brand awareness advertising, and employee salaries and benefits paid to employees engaged in sales and marketing activities.

The increase in sales and marketing expense is attributable to our increased telemarketing hours and direct mail efforts. A large increase occurred in the second quarter as a result of our purchase of Touch 1 in April 2000, and the hiring of additional employees in their existing locations and the opening of a new call center in Canada. Our direct mail campaign was continued through the second quarter of 2000 after its successful introduction in first quarter 2000. We intend to significantly increase our sales and marketing expenditures during the remainder of the year 2000 as we increase our telemarketing and direct mail campaigns and develop other marketing channels.

RESEARCH AND DEVELOPMENT. Research and development expenses increased \$1.4 million to \$1.8 million for the three months ended June 30, 2000, compared to \$0.4 million for the same period in the prior year. Research and development expenses increased \$1.6 million to \$3.1 million for the six months ended June 30, 2000, compared to \$1.5 million for the same period in the prior year. Our research and development expenses consist primarily of salaries and benefits paid to employees engaged in research and development activities and outside third party development costs.

The enhancement of our current product offerings, development of new services, and the integration of our customer care and billing software contributed to increased research and development cost for both the three and six months ended June 30, 2000. We adopted the provisions of Statement of Position (SOP) 98-1 "Accounting for the Cost of Computer Software Developed or Obtained for Internal Use," at the beginning of 1999. As a result, \$1.7 and \$3.7 million of research and development costs relating to development of internal use software were capitalized for the three and six months ended June 30, 2000, compared to \$1.1 and \$2.2 million for the same periods in the prior year. We expect research and development costs to increase in the future as we enhance and develop new services.

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GENERAL AND ADMINISTRATIVE. General and administrative expense increased \$18.5 million to \$20.9 million for the three months ended June 30, 2000,

compared to \$2.4 million for the same period in the prior year. General and administrative expense increased \$26.3 million to \$31.3 million for the six months ended June 30, 2000, compared to \$5.0 million for the same period in the prior year. General and administrative expenses consist primarily of employee salaries, temporary services, bad debt expense, billing and collection expense, occupancy costs, and provisioning costs for Z-Line Home Edition Customers.

The acquisition of Touch 1 and the increase in subscribers has caused an increase in expenses for general and administrative purposes for both the three and six months ended June 30, 2000 compared to the same periods in the prior year. We increased our capacity for back office operations to provide for our anticipated growth and introduction of Z-Line Home Edition to new states. We anticipate general and administrative expenditures will continue to increase in the future as we increase our subscribers, expand our services and enter new states.

DEPRECIATION AND AMORTIZATION. Depreciation and amortization expense increased \$3.5 million to \$4.4 million for the three months ended June 30, 2000, compared to \$0.9 million for the same period in the prior year. Depreciation and amortization expense increased \$4.8 million to \$6.5 million for the six months ended June 30, 2000, compared to \$1.7 million for the same period in the prior year.

The increase in depreciation and amortization is a result of the acquisition of Touch 1 and purchases of equipment. The amortization of the \$67.0 million of intangible assets, constituting the amount of consideration in excess of the fair market value of the net assets purchased from Touch 1, which has been preliminarily allocated to assets with 5 and 20 year lives, resulted in amortization of \$1.2 million in the second quarter of 2000. In addition, the purchase of computer equipment, switching equipment, furniture and leasehold improvements required to maintain our growth and expand our operations has also contributed to the increased depreciation and amortization expense for both the three and six months ended June 30, 2000. We expect depreciation and amortization to continue to increase as we increase our capital expenditures.

INTEREST INCOME. Interest income increased \$0.4 million to \$0.5 million for the three months ended June 30, 2000, compared to \$0.1 million for same period in the prior year. Interest income increased \$1.5 million to \$1.7 million for the six months ended June 30, 2000, compared to \$0.2 million for same period in the prior year. Interest income consists of income on our cash balances invested in short-term liquid investments. The increase was primarily due to larger cash reserves, resulting from funds raised in our initial public offering on December 15, 1999. We raised net proceeds of \$109.1 million after underwriting discounts and commissions. Our cash and cash equivalents were \$10.7 million and \$2.3 million at June 30, 2000 and 1999, respectively.

INTEREST EXPENSE. Interest expense decreased \$0.4 million to \$0.8 million for the three months ended June 30, 2000, compared to \$1.2 million for the same period in the prior year. Interest expense decreased \$0.4 million to \$1.1 million for the six months ended June 30, 2000, compared to \$1.5 million for the same period in the prior year. Our interest expense is a result of the interest charged on our capital lease and other debt obligations. On February 14, 2000, we paid \$14.4 million to extinguish our sale-leaseback credit facility. We anticipate interest expense to increase in the future as a result of our assumption of debt from the Touch 1

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acquisition and the borrowing of money to support operations through our accounts receivable credit facility and possible additional funding prior to the end of fiscal year 2000.

INCOME TAX EXPENSE. No provision for federal or state income taxes has been recorded due to the full valuation allowance recorded against the deferred tax asset for the three and six month periods ended June 30, 2000 and for the same periods in the prior year.

NET LOSS. Our net loss increased \$17.1 million to \$23.1 million for the three months ended June 30, 2000, compared to \$6.0 million for the same period in the prior year. Our net loss increased \$26.3 million to \$38.5 million for the six months ended June 30, 2000, compared to \$12.2 million for the same period in the prior year. This increase was due primarily to the increases in expenses described above.

EBITDA. Many securities analysts use the measure of earnings before deducting interest, taxes, depreciation and amortization, also commonly referred to as "EBITDA," as a way of evaluating a company's financial performance. While EBITDA is not a measure under generally accepted accounting principles, EBITDA is a measure commonly used in the telecommunications industry and is presented to assist in understanding our operating results. Our negative EBITDA increased \$14.7 million to \$18.3 million for the three months ended June 30, 2000, compared to \$3.6 million for the same period in the prior year. Our negative EBITDA increased \$24.0 million to \$32.7 million for the six months ended June 30, 2000, compared to \$8.7 million for the same period in the prior year. We expect to experience a reduction in negative EBITDA during the remainder of fiscal year 2000 as a result of our increases in subscribers.

LIQUIDITY AND CAPITAL RESOURCES

The competitive local telecommunications service business is traditionally considered to be a capital intensive business owing to the significant investments required in fiber optic communication networks and the co-location of switches and transmission equipment in incumbent local exchange carriers' central offices. Our network architecture is designed with remotely located points of presence, or Z-Nodes, that can be interconnected through local and long distance communications networks to the Z-Tel enterprise management center. We do not expect that the growth of our business will require the levels of capital investment in fiber optics and switches that existed in historical telecommunications models. Instead, we will devote significant amounts of our capital resources to continued operations, software development and marketing efforts that we have designed to achieve rapid penetration of our target markets.

We have incurred accumulated losses since our inception as a result of developing our business, research and development, building and maintaining network infrastructure and technology, sales and promotion of our services, and administrative expenditures. As of June 30, 2000, we had an accumulated deficit of \$87.6 million. We have funded these expenditures primarily through operating revenues, private securities offerings, a sale-leaseback credit facility and an initial public offering of 6.9 million shares of common stock (including the underwriters' over-allotment option) that raised net proceeds of \$109.1 million after underwriting discounts and commissions. We intend to continue building our organization in anticipation of future growth and believe that our operating expenditures will also continue to increase.

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On April 14, 2000, we completed the acquisition of Touch 1 for approximately \$9.0 million in cash and 1.1 million shares of our common stock. The Touch 1 acquisition was accounted for using the purchase method of accounting. The acquisition of Touch 1 resulted in \$67.0 million of intangible assets preliminarily being allocated to assets being amortized over 5 and 20 years.

The Company also has entered into an agreement with a service firm to provide various content and new service offerings through the telephone. Under this agreement Z-Tel has invested \$3.0 million and is committed to an additional \$4.0 million in cash payments for future services. This contract provides for early termination under certain circumstances with adjustments to the commitments.

In August 2000, the Company entered into an agreement with a service firm to outsource customer provisioning through electronic bonding with incumbent

local exchange carriers. Under this agreement Z-Tel is committed to \$0.5 million cash payment for set-up fees and minimum commitment fees for the next three years, subject to the service firm attaining certain milestones in the future. The minimum commitments under the contract, subject to certain adjustments, are \$4.0, \$7.0, and \$9.0 million over the next three years. This contract provides for various termination arrangements with related severance fees.

NET CASH USED IN OPERATING ACTIVITIES. Net cash used in operating activities increased by \$31.0 million to \$42.1 million for the six months ended June 30, 2000, compared to \$11.1 million for the same period in the prior year. Our increase in cash used in operating activities increased was primarily because of increasing net losses.

NET CASH USED IN INVESTING ACTIVITIES. Net cash used in investing activities was \$30.2 million for the six months ended June 30, 2000, compared to \$3.7 million provided by investing activities for the same period in the prior year, a change of \$33.9 million. For the six months ended June 30, 2000, we invested \$9.0 million in cash to acquire Touch 1 and purchased property and equipment of \$20.2 million. For the six months ended June 30, 1999, we received \$9.9 million in a sale and leaseback transaction and purchased property and equipment of \$6.2 million.

The increase in net cash used in investing activities is a direct result of our continued preparation for rapid growth and our plans to lower network and infrastructure costs. In 2000, we are focused on product development and the establishment of our infrastructure, the operation of our technology and a network that primarily involves the purchases of equipment for our Z-Nodes. As discussed earlier, the purchase of Touch 1 has greatly increased our back office operations. We have increased our employees at all locations including our newest call center in Canada. The increase in employees coupled with our increase in subscribers has required us to make capital investments in switching equipment, computer equipment, software, leasehold improvements, and office equipment to provide for our growing employee and subscriber base.

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NET CASH USED IN FINANCING ACTIVITIES. Net cash used in financing activities was \$18.8 million for the six months ended June 30, 2000, compared to net cash provided by financing activities of \$1.6 million for the same period in the prior year, a change of \$20.4 million. The overall change is primarily attributable to our payment of \$23.1 million during the second quarter of 2000 for the extinguishment of debt. We extinguished our sale-leaseback credit facility, assumed debt from the Touch 1 acquisition relating to a line of credit and paid off a lease obligation in the amounts of \$14.4, \$1.0 and \$3.5 million, respectively. The remaining payments on long-term debt and capital lease obligations are the debt service for the debt assumed from the Touch 1 acquisition. On February 14, 2000, we paid \$14.4 million to extinguish the outstanding CMB Capital, LLC capital lease obligation and purchase the related assets. This was the repayment of transactions involving the sale and leaseback of various furniture and equipment payable over four years from the date of the transactions. This transaction accounted for a \$1.6 million increase in the carrying value of our assets, resulting from the payments made to terminate the lease and the carrying value of our capital lease obligation. This \$1.6 million was added to the value of the assets purchased and is depreciated over the estimated remaining lives in accordance with FASB Interpretation No. 26 - Accounting for Purchase of a Leased Asset by the Lessee during the Term of the Lease, an interpretation of FASB Statement No. 13. The cash used in financing activities was offset by the receipt of payments of cash for notes receivable from stockholders for common stock and cash received for

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the exercise of stock options, in the amounts of \$1.1 and \$1.3 million, respectively, for the six months ended June 30, 2000.

In July 2000, we filed a Certificate of Designation authorizing the issuance of 5.0 million shares of Series D convertible preferred stock ("Series D Preferred"). We have received commitments to purchase 4,688,247 shares of the Series D Preferred at a price of \$12.00 for aggregate proceeds of \$56.3 million, \$43.1 million of which have been received by us. The Series D Preferred is convertible at a conversion price of \$12.00, which price is subject to adjustment into common stock at the option of the holder (i.e., initially convertible on a one-for-one basis); however, there are certain circumstances that provide for a forced conversion of the stock by us. The Series D Preferred is mandatorily redeemable 8 years from the original issue date, has an 8% cumulative dividend payable at times in cash and at times with in-kind contributions of additional Series D Preferred and has certain liquidation preferences and voting rights. Each purchaser of Series D Preferred received a warrant to purchase a number of shares of our common stock equal to one-half of the amount of Series D Preferred purchased by each investor. Each warrant is exercisable at a price of \$13.80 per share subject to certain adjustments.

In July 2000, we entered into an accounts receivable facility with RFC Capital Corporation ("RFC") providing for the sale of certain of our accounts receivable to RFC. RFC has agreed to purchase up to \$25 million of our accounts receivable, \$10 million of which is subject to our meeting certain conditions, with provisions for a commitment of up to \$50 million, subject to successful syndication of the receivables sales program by RFC. We have not utilized any of this facility to date. In connection with this agreement, we have granted RFC a security interest in our accounts, lists, agreements, letter of authorizations, contract rights, instruments, documents, chattel paper, general intangibles, and all proceeds of the foregoing. The annual interest rate equivalent charged to us under this agreement floats at prime rate plus 2.0% to 2.5%, depending upon the nature of receivables sold.

Our ongoing capital requirements will depend on several factors, including market acceptance of our services, the amount of resources we devote to investments in our networks, facilities, build-out of additional enterprise management centers, services development and brand promotions, the resources we devote to sales and marketing of our services, and other factors. We have experienced a substantial increase in our capital expenditures and operating losses since our inception consistent with the growth in our operations and staffing, and we anticipate that this will continue for the foreseeable future. Additionally, we expect to make additional investments in technologies and our network architecture, and plan to expand our sales and marketing programs and conduct more brand promotions. Although operating activities may provide cash in certain periods, to the extent we experience growth in the future, we anticipate that our operating and investing activities will use cash. As of June 30, 2000, we had \$10.7 million in cash and cash equivalents. We believe that cash on hand combined with our recent offering of Series D Convertible Preferred Stock for a total committed amount of \$56.3 million and the up to \$50 million potentially available under the RFC Capital Corporation accounts receivable facility will be sufficient to meet our projected capital requirements through the end of fiscal year 2000. Nevertheless, to address new opportunities that the Company has identified internally and other opportunities that have been presented to Z-Tel, it is possible that additional funding will be necessary. Consequently, we may need to obtain additional equity or debt financing which may not be available on attractive terms, or at all, or may be dilutive. If we are not able to obtain such financing or obtain it on terms that are not attractive, we may be required to modify, delay or abandon our current business plan, which is likely to materially and adversely affect our business.

YEAR 2000 COMPLIANCE

We did not experience any significant disruptions in our operations during the transition into the Year 2000. We believe we have completed necessary assessments, modifications or replacement and testing of systems critical for the delivery of our services. We believe our Year 2000 readiness objectives have been met. We also prepared a contingency plan to mitigate potential adverse effects that might have arisen from non-compliant systems or third parties that had not adequately addressed the Year 2000 issue. While we did not experience any significant Year 2000 disruptions during the transition into the Year 2000,

we will continue to monitor our operations and systems and address any date-related problems that may arise.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We currently have instruments sensitive to market risk relating to exposure to changing interest rates and market prices. We do not enter into financial instruments for trading or speculative purposes and do not currently utilize derivative financial instruments. Our operations are conducted primarily in the United States and as such are not subject to material foreign currency exchange rate risk.

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 short-term nature of the major portion of our investment portfolio.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

1. Civil Action File No. 8:00 CV-1148-T-24B; PTEK HOLDINGS, INC., F/K/A PREMIERE TECHNOLOGIES, INC., AND PREMIERE COMMUNICATIONS, INC. V. Z-TEL TECHNOLOGIES, INC., Z-TEL COMMUNICATIONS, INC., DAVID GREGORY SMITH, JAMES KITCHEN AND EDUARD MAYER; in the United States District Court for the Middle District of Florida, Tampa Division.

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On June 9, 2000, PTEK Holdings, Inc. and Premiere Communications, Inc. (collectively, "PTEK") filed a lawsuit against Z-Tel Technologies, Inc. ("Z-Tel"), Z-Tel Communications, Inc., David Gregory Smith, Z-Tel's Chairman, Chief Executive Officer and President, Eduard Mayer, one of Z-Tel's directors and James Kitchen, a Senior Vice President of Z-Tel. In the lawsuit, PTEK claims that the defendants have infringed and are continuing to infringe a patent that purports to, among other things, describe a method for enabling a user to manipulate data underlying a web site using a telephone, and have misappropriated and are continuing to misappropriate trade secrets belonging to PTEK, particularly those relating to a unified messaging platform, that Messrs. Smith and Kitchen breached contractual obligations owed to PTEK by, among other things, misappropriating PTEK's trade secrets and improperly soliciting PTEK's customers and employees, that the defendants have engaged in unfair competition, that the defendants have converted PTEK's physical and intellectual property, that Messrs. Smith, Kitchen and Mayer misappropriated corporate opportunities of PTEK, that the defendants conspired to misappropriate corporate opportunities of PTEK, and that the defendants tortiously interfered with contractual relations between PTEK and its employees and with PTEK's actual and prospective business relationships. PTEK seeks preliminary and permanent injunctive relief against the defendants, an equitable trust of an unspecified amount of common stock of Z-Tel, return of proceeds, with interest, of moneys realized by Mr. Smith from the exercise and sale of PTEK options, disgorgement of economic benefits wrongfully obtained, an unspecified amount of actual and punitive damages arising out of the common law claims, treble damages for willful infringement of the PTEK patent and costs. The defendants believe the claims asserted in the lawsuit are without merit and intend to defend it vigorously.

The corporate defendants have answered the complaint and have filed counterclaims against PTEK and Boland Jones ("Jones"), its Chairman and Chief Executive Officer. The counterclaims allege that PTEK and Jones tortiously interfered with actual and prospective business relationships between Z-Tel and certain investment bankers, defamed Z-Tel and made false and defamatory statements to Z-Tel while knowing or having a reason to know that they would be disclosed to third parties. PTEK and Jones have moved to dismiss Z-Tel's counterclaims, and Z-Tel has filed a response. The Court has not ruled on PTEK's and Jones' motion.

PTEK also has filed motions for a preliminary injunction and for expedited discovery. Z-Tel has responded to each of those motions, and the Court has denied PTEK's motion for expedited discovery without prejudice on the ground that it failed to comply with certain of the Court's local rules. PTEK has submitted further briefing on these issues, but the Court has not issued any further rulings or set any hearing on PTEK's motion for preliminary injunction.

2. Case No. 98-12260; IN RE TOUCH 1 COMMUNICATIONS, INC.; in the United States Bankruptcy Court for the Southern District of Alabama

Case No. 98-12402; IN RE DIRECTEL; in the United States Bankruptcy Court for the Southern District of Alabama

Touch 1 Communications, Inc. ("Touch 1") and its wholly owned subsidiary, directTEL, Inc. ("directTEL") (collectively, the "Debtors"), filed voluntary petitions for relief under chapter 11 of the Bankruptcy Code on June 29, 1999 and July 9, 1999, respectively, in the United States

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Bankruptcy Court for the Southern District of Alabama (the "Bankruptcy Court"). The Debtors proposed their Joint Plan of Reorganization of Touch 1 Communications, Inc. and directTEL, Inc. under Chapter 11 of the United States Bankruptcy Code (the "Plan"), which received overwhelming acceptance by the Debtors' creditors. On August 6, 1999, the Bankruptcy Court entered an Order Confirming Amended Joint Plan of Reorganization of Touch 1 Communications, Inc. and directTEL, Inc. Under Chapter 11 of the United States Bankruptcy Code (the "Confirmation Order"). As a result, the Debtors were discharged of certain obligations except as provided for in the Plan.

Since the entry of the Confirmation Order, the Debtors' activities in the Bankruptcy Court have been limited to resolving contested claims. On or about August 3, 2000, directTEL filed a pleading with the Bankruptcy Court to close its bankruptcy case, and it is anticipated that Touch 1's bankruptcy case will be closed during the third quarter of 2000.

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS.

RECENT SALES OF UNREGISTERED SECURITIES

During the period covered by this report, Z-Tel sold, in connection with the closing of its acquisition of Touch 1 Communications, Inc., in the aggregate, 1,100,000 shares of its common stock to the holders of the outstanding common and preferred stock of Touch 1 Communications, Inc. who executed the definitive agreement relating to the acquisition. Z-Tel claims an exemption from registration under Section 4(2) of the Securities Act of 1933 because such transactions were by an issuer and did not involve a public offering.

USE OF PROCEEDS FROM INITIAL PUBLIC OFFERING

Z-Tel filed a registration statement (Commission file no. 333-89063), which became effective on December 14, 1999, with respect to the initial public offering of 6,900,000 shares of its common stock (including the underwriters' over-allotment option). For the six months ended June 30, 2000, approximately \$67.4 million of the net offering proceeds were used in the following estimated amounts and for the following purposes: \$6.4 million for the purchase and installation of network equipment, \$7.0 million for the purchase of software and support and software development, \$4.3 million for marketing expenses, \$19.9 million for the repayment of indebtedness, \$26.6 million for operational expenses, \$2.1 million for construction of plant, building and facilities and \$1.1 million for the purchase of investments. The remaining offering proceeds have been placed in temporary investments in cash and cash equivalents. Except for dividend payments made to entities affiliated with our directors based on their pro rata ownership of our convertible preferred stock, none of the net offering proceeds have been paid, directly or indirectly, to our directors,

officers, 10% shareholders or affiliates.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

At the Annual Meeting of Shareholders held on May 30, 2000, the following proposals were adopted by the margins indicated:

1. To elect a Board of Directors to hold office until their successors are elected and qualified:

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	For	Number of Shares Withheld
Laurence S. Grafstein	24,730,914	120,473
Eduard J. Mayer	24,730,914	120,473
Buford H. Ortale	24,730,914	120,473
Jeffrey A. Bowden	24,730,914	120,473
D. Gregory Smith	24,730,914	120,473

2. To approve the second amendment to Z-Tel's Amended and Restated Certificate of Incorporation classifying the Board of Directors of Z-Tel:

For: 20,453,916
Against: 3,282,631
Abstain: 374

3. To approve the 2000 Equity Participation Plan of Z-Tel:

For: 20,034,388
Against: 3,636,054
Abstain: 66,479

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(A) EXHIBITS.

The following exhibits are filed as part of this report:

Exhibit Number -----	Description -----
2.1(**)	Agreement and Plan of Merger dated April 10, 2000 by and among Z-Tel Technologies, Inc., Tiger Acquisition Subsidiary, Inc., Touch 1 Communications, Inc., and certain shareholders of Touch 1 Communications, Inc.
3.1(***)	Amended and Restated Certificate of Incorporation of Z-Tel, as amended
3.2(*)	Amended and Restated Bylaws of Z-Tel
4.1(*)	Form of Common Stock Certificate
4.2	See Exhibits 3.1 and 3.2 for provisions of the Amended and Restated Certificate of Incorporation, as amended, and the amended and restated Bylaws of Z-Tel defining rights of security holders

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- 4.3 Stock Purchase Agreement, dated July 6, 2000, by and between the Registrant and the various purchasers of the Registrant's Series D Convertible Preferred Stock
- 4.4 Certificate of Designations, Preferences and Relative Rights, Qualifications, Limitations and Restrictions relating to the Registrant's Series D Convertible Preferred Stock.
- 4.5 Registration Rights Agreement by and between the Registrant and each of the purchasers of the Registrant's Series D Convertible Preferred Stock.
- 4.6 Form of Warrant for the purchase of shares of common stock of Z-Tel Technologies, Inc. by each of the purchasers of the Registrant's Series D Convertible Preferred Stock.
- 10.1.1(*) Stockholders' Agreement dated October 8, 1999, between and among the company, BA Capital Corporation, Sewanee Partners II, L.P., Gramercy Z-Tel LLC and the other parties set forth therein
- 10.1.2(*) Employment Agreement dated July 1998 between the Company and D. Gregory Smith
- 10.1.3(*) Employment Agreement dated September 1999 between the Company and John Hutchens
- 10.1.4(*) Employment Agreement dated August 1998 between the Company and Charles W. McDonough
- 10.1.5(*) Employment Agreement dated August 1998 between the Company and J. Bryan Bunting
- 10.1.6(*) Employment Agreement dated July 1998 between the Company and James A. Kitchen
- 10.1.7(*) Investment Agreement dated March 15, 1999 between the Company and CMB Capital LLC
- 10.2.1(*) 1998 Equity Participation Plan
- 10.2.2(****) 2000 Equity Participation Plan
- 10.3(**) Form of Employment Agreement for certain key Touch 1

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employees, including James F. Corman,
President of Touch 1

Z-TEL COMMUNICATIONS, INC

Exhibit D

Profiles of Senior Management Key Personnel

Z-Tel Communications, Inc.

MANAGERIAL AND TECHNICAL CAPABILITIES

D. Gregory Smith

Mr. Smith is a founder of the Company and has served as a Director, President and Chief Executive Officer since its inception in January 1998. Mr. Smith was a director of Premiere Technologies, Inc. from 1991 to 1997, executive vice president from 1994 to 1997 and vice president from 1991 to 1994. From 1987 to 1991, Mr. Smith was a management and financial consultant with Olympus Telecommunications, Inc. and Olympus Partners, Inc., companies that he founded. Mr. Smith has also held positions with NationsBank of Florida, N.A. and Chase Bank of Florida. Mr. Smith received his B.S. in Commerce from the University of Virginia.

James F. Corman

Mr. Corman is President of the Consumer Services division for Z-Tel Communications, Inc. and has served in this capacity since April, 2000. Prior to accepting this position, and from 1989-April, 2000, Mr. Corman was President of Touch 1 Communications, a nationwide long distance company, now a wholly owned subsidiary of Z-Tel Technologies, Inc. Prior to Touch 1, Mr. Corman was Senior Vice President with Telecom USA, at that time the fourth largest long distance company in the U.S. Mr. Corman began his career in telecommunications in 1969 holding various positions within Southland Communications corporation, including President from 1981-1987. Mr. Corman holds a B.S. from Auburn University and an M.B.A. from the University of Texas.

John M. Hutchens

Mr. Hutchens has served as Senior Vice President - Chief Financial Officer since September 1999. From 1982 through 1999 he was an employee and then a partner at Arthur Anderson LLP. Mr. Hutchens received a B.S. in Accountancy from the University of Illinois, and a Masters of Health Administration from the Ohio State University. Mr. Hutchens is a Certified Public Accountant licensed in Florida.

Charles W. McDonough

Mr. McDonough has served as Senior Vice President - Chief Technology Officer since August 1998. From 1975 through 1998, he was an employee and then a partner at Anderson Consulting LLP. Mr. McDonough received a B.A. in Industrial Engineering and a M.S. in Industrial Administration from Carnegie Mellon University.

J. Bryan Bunting

Mr. Bunting has served as Senior Vice President - Engineering and Technical Services since January 1999. Mr. Bunting served as senior vice president - Z-Tel Business Networks from August 1998 to January 1999. From 1968 through 1998, he was an officer of NationsBank, serving most recently as senior vice president of direct banking. Mr. Bunting attended Old Dominion University.

Mark H. Johnson

Mr. Johnson has served as Secretary and Treasurer of Z-Tel since August 1999. From May 1998 until his Z-Tel at Z-Tel, Mr. Johnson was an employee of Olympus Management, a venture firm. From 1991 until 1998, Mr. Johnson was an employee of First Union National Bank. Mr. Johnson holds a B.A. from the University of Virginia.

Robert A. Curtis

Mr. Curtis has served as Senior Vice President - Strategic Planning since July 1999. From May 1998 to June 1999, Mr. Curtis was Vice President - Business Development and Legal Affairs at Z-Tel. From September 1995 to April 1998, Mr. Curtis was an attorney at the Houston office of Fulbright & Jaworski, LLP, where he specialized in antitrust and complex federal litigation. Mr. Curtis graduated from the Duke University School of Law in 1995; received his B.A. in Philosophy from Trinity University and his Doctor of Philosophy from the University of Oxford, England.

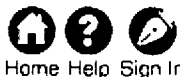
Doug W. Jackson

Mr. Jackson has served as Vice President - Marketing of Z-Tel since June 1999. From 1996 through 1999 he held the position of senior brand manager for the Coca-Cola Company and prior to that from 1992 to 1996 he was an associate product manager for Kraft General Foods Corp. Mr. Jackson received his B.A. from the University of Virginia and his M.B.A. from the University of Michigan.

Z-TEL COMMUNICATIONS, INC

Exhibit E

Press Release



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Z-Tel Technologies Inc. (ticker: ZTEL, exchange: NASDAQ) News Release - 18-Oct-2000

Z-Tel Subscriber Base Grows to 256,000 At End of the Third Quarter, Up 51% Sequentially From Second Quarter

TAMPA, Fla.--(BUSINESS WIRE)--Oct. 18, 2000--

Company Hits Upwardly Revised Estimate Despite Widespread

Verizon Strike During Quarter

Gregg Smith, Chief Executive Officer of Z-Tel Technologies, Inc. (Nasdaq/NMS:ZTEL), today announced that the Company's base of Z-Line Home Edition subscribers has increased 51% during the last three months to end the third quarter of 2000 at 256,000, compared with 170,000 at the end of the second quarter. As a result of Z-Tel's continued substantial growth in subscribers, the Company expects to post strong financial results for the third quarter of 2000.

Mr. Smith remarked, "Z-Tel has continued its extraordinary growth for the latest quarter, adding more than 80,000 new subscribers for the second consecutive quarter. We accomplished this performance in spite of the unanticipated provisioning delays resulting from the strike against Verizon Communications in New York, our single largest market. We believe our results for the quarter continue to demonstrate the strong demand for our Z-Line, which is an innovative, internet-enhanced alternative to traditional phone service.

"Significantly, the great majority of our new subscribers came from the four states in which we were already operating at the beginning of the quarter - New York, Texas, Massachusetts and Pennsylvania - and which also represent an aggregate market of approximately 22 million potential subscribers. We have doubled the size of our potential market since the start of the third quarter to approximately 44 million potential subscribers by entering Georgia, Maryland, Oregon, California and Illinois. We continue to expect to open additional territory during the fourth quarter."

John Goeres, Senior Vice President for Business Operations, added "Our consistent ability to meet or exceed our business objectives throughout this fiscal year has been dependent on the continuing growth of our back-office operations, which have tripled in capacity in the past year. In passing the quarter-million subscriber milestone, we have once again made a strong statement about the appeal of Z-Line and Z-Tel's ability to provision and service its subscribers. Despite a difficult industry environment, Z-Tel has accomplished its operational and financial goals, solidified its entry into new markets and validated its systems design

and operation."

About Z-Tel Technologies, Inc.(TM)

Z-Tel Technologies, Inc. provides consumers bundled local and long distance telephone services, combined with enhanced, Internet-based communications features that enable them to manage all of their voice communications needs. Z-Tel currently sells this bundle as "Z-Line Home Edition(TM)" in nine states, including New York, Texas, Massachusetts, Pennsylvania, Georgia, Oregon, Maryland, California and Illinois, and had 256,000 active customers at the end of the third quarter. For more information about this innovative new service or about Z-Tel, please visit the Company's web site at www.z-tel.com.

Z-Tel Technologies, Inc., Z-Line and Z-Line Home Edition are trademarks of Z-Tel Technologies, Inc.

This press release contains forward-looking statements that are based upon current expectations and involve a number of risks and uncertainties. In order for Z-Tel to utilize the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, you are hereby cautioned, and Z-Tel hereby notes, that these statements may be affected by the risk that favorable growth and financial trends may not continue; the risk that the Company will be unable to efficiently and successfully enter new markets, including those set forth in this release, in the specified time frame or at all, the risk that the Company's existing financing will not be sufficient to fund anticipated growth and that additional financing may not be available on favorable terms or at all, and the risk that further state market and financial expansion may not be achieved, as well as the risk factors described in detail in Z-Tel's 1999 Annual Report on Form 10-K, filed March 28, 2000; and in Z-Tel's other filings with the Securities and Exchange Commission. Z-Tel undertakes no obligation to update or revise any such forward-looking statements.

CONTACT: Z-Tel Technologies Inc., Tampa

Mark H. Johnson, 813/233-4610

mjohnson@z-tel.com

Z-TEL COMMUNICATIONS, INC

Exhibit F

Proposed Service Area Map

Z-Tel intends to offer service throughout the State of North Dakota. The company initially will offer service in territory currently served by Qwest Corporation.

Z-TEL COMMUNICATIONS, INC

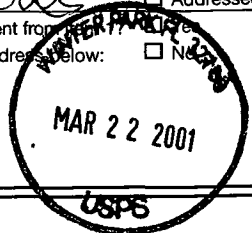
Exhibit G

Carriers Offering Similar Services

To the best of Applicant's knowledge and information, the list of other public utilities providing similar service in the State of North Dakota coincides with the list of competitive local exchange carriers (CLECs) which are registered with the North Dakota Public Service Commission, plus incumbent local exchange carriers serving the state (eg: Qwest Corporation). A list of CLECs registered with the Commission is provided in this exhibit.

PU-2079-00-655

SENDER: COMPLETE THIS SECTION		COMPLETE THIS SECTION ON DELIVERY	
<ul style="list-style-type: none"> Complete items 1, 2, and 3. Also complete item 4 if Restricted Delivery is desired. Print your name and address on the reverse so that we can return the card to you. Attach this card to the back of the mailpiece, or on the front if space permits. 		A. Received by (Please Print Clearly) Jackie Harris	B. Date of Delivery 3/22/01
1. Article Addressed to: Monique Byrnes Technologies Management PO Drawer 200 Winter Park FL 32790-0200		C. Signature <i>Jackie Harris</i>	<input type="checkbox"/> Agent <input type="checkbox"/> Addressee
		D. Is delivery address different from item 1? If YES, enter delivery address below: <input type="checkbox"/> No	
2. Article Number (Copy from service label) 7000 0520 0022 0773		3. Service Type <input checked="" type="checkbox"/> Certified Mail <input type="checkbox"/> Express Mail <input type="checkbox"/> Registered <input type="checkbox"/> Return Receipt for Merchandise <input type="checkbox"/> Insured Mail <input type="checkbox"/> C.O.D.	
PS Form 3811, July 1999		Domestic Return Receipt	



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SENDER: COMPLETE THIS SECTION		COMPLETE THIS SECTION ON DELIVERY	
<ul style="list-style-type: none"> Complete items 1, 2, and 3. Also complete item 4 if Restricted Delivery is desired. Print your name and address on the reverse so that we can return the card to you. Attach this card to the back of the mailpiece, or on the front if space permits. 		A. Received by (Please Print Clearly) R. DORIA	B. Date of Delivery 12-27-00
1. Article Addressed to: Monique Byrnes Technologies Management PO Drawer 200 Winter Park FL 32790-0200		C. Signature <i>R. Doria</i>	<input type="checkbox"/> Agent <input type="checkbox"/> Addressee
		D. Is delivery address different from item 1? If YES, enter delivery address below: <input type="checkbox"/> No	
2. Article Number (Copy from service label) 7000 0520 0022 8653 3010		3. Service Type <input checked="" type="checkbox"/> Certified Mail <input type="checkbox"/> Express Mail <input type="checkbox"/> Registered <input type="checkbox"/> Return Receipt for Merchandise <input type="checkbox"/> Insured Mail <input type="checkbox"/> C.O.D.	
PS Form 3811, July 1999		Domestic Return Receipt	

PU-1544-00-655

SENDER: COMPLETE THIS SECTION		COMPLETE THIS SECTION ON DELIVERY	
<ul style="list-style-type: none"> Complete items 1, 2, and 3. Also complete item 4 if Restricted Delivery is desired. Print your name and address on the reverse so that we can return the card to you. Attach this card to the back of the mailpiece, or on the front if space permits. 		A. Received by (Please Print Clearly) Ricardo Lattimore	B. Date of Delivery
1. Article Addressed to: Monique Byrnes Technologies Management PO Drawer 200 Winter Park FL 32790-0200		C. Signature <i>Ricardo Lattimore</i>	<input type="checkbox"/> Agent <input type="checkbox"/> Addressee
		D. Is delivery address different from item 1? If YES, enter delivery address below: <input type="checkbox"/> No	
2. Article Number (Copy from service label) 7000 0520 0022 8563 3034		3. Service Type <input type="checkbox"/> Certified Mail <input type="checkbox"/> Express Mail <input type="checkbox"/> Registered <input type="checkbox"/> Return Receipt for Merchandise <input type="checkbox"/> Insured Mail <input type="checkbox"/> C.O.D.	
PS Form 3811, July 1999		Domestic Return Receipt	