

# OFFERING CIRCULAR



US\$190,000,000

**Axtel, S.A.B. de C.V.**

**9.0% Senior Unsecured Notes due 2019**

We are offering US\$190,000,000 aggregate principal amount of our 9.0% Senior Unsecured Notes due 2019 (the "new notes"). The new notes are being offered as additional debt securities under an indenture pursuant to which we have previously issued US\$300.0 million aggregate principal amount of 9.0% Senior Unsecured Notes due 2019. The US\$300.0 million 9.0% Senior Unsecured Notes due 2019 that we previously issued are referred to as the "existing notes." As used herein the term "notes" refers to both the new notes and the existing notes. The new notes will be treated as a single series with the existing notes and will have the same terms as those of the existing notes. The new notes and the existing notes will vote as one class under the indenture governing the notes. Immediately after giving effect to the issuance of the new notes offered by this offering circular, we will have US\$490.0 million aggregate principal amount of our 9.00% Senior Unsecured Notes due 2019. We will pay interest on the new notes semi-annually on each March 22 and September 22, commencing on September 22, 2010. The new notes will mature on September 22, 2019. Prior to September 22, 2012, we may redeem up to 35% of the notes using proceeds from one or more equity offerings. Prior to September 22, 2014, we may redeem some or all of the notes at a redemption price equal to 100.0% of the principal amount, plus accrued and unpaid interest, if any, plus the "make-whole" premium described in this offering circular. In addition, we may redeem some or all of the notes on or after September 22, 2014 at the redemption prices set forth in this offering circular. There is no sinking fund for the notes.

The new notes, together with the existing notes, will be our senior unsecured obligations, will rank equally in right of payment with our existing and future senior unsecured indebtedness, including the existing notes, and will be senior in right of payment to any of our future subordinated indebtedness. The new notes will be effectively junior to all of our existing and future secured indebtedness to the extent of the assets securing that indebtedness and all other indebtedness owed to statutorily preferred creditors. Except for Telecom Networks Inc., each of our current and certain of our future subsidiaries will unconditionally guarantee the notes, jointly and severally, on a senior unsecured basis. These guarantees will rank equally with all existing and future senior unsecured obligations of the guarantors, including the existing notes, and will be effectively subordinated to existing and future secured indebtedness of the guarantors to the extent of the assets securing that indebtedness and all other indebtedness owed to statutorily preferred creditors.

No public market currently exists for the new notes. We have applied to list the new notes on the Official List of the Luxembourg Stock Exchange and for trading on the Euro MTF market. See "Listing and General Information."

**Investing in the new notes involves risks. See "Risk Factors" beginning on page 13.**

**Price: 102.5%**

**plus accrued interest, if any, from March 22, 2010.**

Delivery of the new notes in book-entry form will be made on or about March 22, 2010.

The new notes have not been registered under the Securities Act of 1933, as amended. The new notes may not be offered or sold within the United States or to U.S. persons, except to qualified institutional buyers in reliance on the exemption from registration provided by Rule 144A and to certain persons in offshore transactions in reliance on Regulation S. You are hereby notified that sellers of the new notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A. For more information on transfer of the new notes see "Transfer Restrictions" beginning on page 150.

**THE NEW NOTES HAVE NOT BEEN AND WILL NOT BE REGISTERED WITH THE NATIONAL SECURITIES REGISTRY (REGISTRO NACIONAL DE VALORES) MAINTAINED BY THE NATIONAL BANKING AND SECURITIES COMMISSION (THE COMISION NACIONAL BANCARIA Y DE VALORES, OR CNBV), AND MAY NOT BE OFFERED OR SOLD PUBLICLY, OR OTHERWISE BE THE SUBJECT OF BROKERAGE ACTIVITIES, IN MEXICO, EXCEPT PURSUANT TO A PRIVATE PLACEMENT EXEMPTION SET FORTH UNDER ARTICLE 8 OF THE LEY DEL MERCADO DE VALORES (THE "MEXICAN SECURITIES MARKET LAW"). AS REQUIRED UNDER THE MEXICAN SECURITIES MARKET LAW, WE WILL NOTIFY THE CNBV OF THE OFFERING OF THE NEW NOTES OUTSIDE OF MEXICO. SUCH NOTICE WILL BE DELIVERED TO THE CNBV TO COMPLY WITH A LEGAL REQUIREMENT AND FOR INFORMATION PURPOSES ONLY, AND THE DELIVERY TO AND THE RECEIPT BY THE CNBV OF SUCH NOTICE DOES NOT IMPLY ANY CERTIFICATION AS TO THE INVESTMENT QUALITY OF THE NEW NOTES OR OUR SOLVENCY, LIQUIDITY OR CREDIT QUALITY. THE INFORMATION CONTAINED IN THIS PRELIMINARY OFFERING CIRCULAR OF THE NEW NOTES IS EXCLUSIVELY THE RESPONSIBILITY OF THE COMPANY AND HAS NOT BEEN REVIEWED OR AUTHORIZED BY THE CNBV. IN MAKING AN INVESTMENT DECISION, ALL INVESTORS, INCLUDING ANY MEXICAN INVESTORS WHO MAY ACQUIRE NEW NOTES FROM TIME TO TIME, MUST RELY ON THEIR OWN REVIEW AND EXAMINATION OF THE COMPANY.**

Joint Book-Running Managers

**Credit Suisse**

**BofA Merrill Lynch**

The date of this confidential offering circular is March 11, 2010.



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**You should rely only on the information contained in this document. We have not authorized anyone to provide you with information that is different or additional information. This document may only be used where it is legal to sell these securities. The information in this document may only be accurate on the date of this document.**

## NOTICE TO INVESTORS

The new notes will be available in book-entry form only. We expect that the new notes sold pursuant to this offering circular will be issued in the form of one or more global certificates which will be deposited with, or on behalf of, The Depository Trust Company (“DTC”), and registered in its name or in the name of Cede & Co., its nominee. Beneficial interests in the global certificates will be shown on, and transfers of the global certificates will be effected only through, records maintained by DTC and its participants. After the initial issuance of the global certificates, new notes in certificated form will be issued in exchange for the global certificates only as set forth in the indenture governing the new notes. See “Description of the Notes—Book-Entry; Delivery and Form.”

This offering circular is being furnished by us on a confidential basis in connection with an offering exempt from registration under the Securities Act and applicable state securities laws solely for the purpose of enabling a prospective investor to consider the purchase of the new notes. Delivery of this offering circular to any other person or any reproduction of this offering circular, in whole or in part, without our or the initial purchasers’ prior consent is prohibited. The information contained in this offering circular has been provided by us and other sources identified herein. No representation or warranty, express or implied, is made by the initial purchasers as to the accuracy or completeness of the information contained in this offering circular, and nothing contained in this offering circular is, or shall be relied upon as, a promise or representation by the initial purchasers.

This offering circular contains summaries, believed to be accurate in all material respects, of terms of various agreements, but reference is made to the actual agreements, copies of which will be made available to you upon request as indicated under “Additional Information.” All such summaries are qualified in their entirety by this reference.

The new notes offered in this offering circular are subject to restrictions on transferability and resale and may not be transferred or resold except as permitted under the Securities Act of 1933, as amended, and applicable state securities laws pursuant to registration or exemption from those laws. You should be aware that you may be required to bear the financial risk of this investment for an indefinite period of time. See “Risk Factors—Risks Relating to the New Notes—An active trading market may not develop for the new notes, which may limit your ability to resell them.”

You must comply with all applicable laws and regulations in force in any jurisdiction in connection with the distribution of this offering circular and the offer or sale of the new notes. For more details, see “Transfer Restrictions.” In making an investment decision, you must rely on your own review of our business and related matters and the terms of this offering, including the merits and risks involved. You should not construe the contents of this offering circular as legal, business or tax advice. You should consult your attorney, business advisor or tax advisor as to legal, business or tax advice.

The new notes offered in this offering circular have not been recommended by the U.S. Securities and Exchange Commission (“SEC”), any state or foreign securities commission or any regulatory authority. The authorities have not confirmed the accuracy or determined the adequacy of this offering circular. Any representation to the contrary is a criminal offense.

We are entitled to withdraw this offering at any time before closing. We are making this offering subject to the terms described in this offering circular and the purchase agreement relating to the new notes.

The new notes offered in this offering circular have not been and will not be qualified for sale under the securities laws of any province or territory of Canada. The new notes are not being offered and may not be offered or sold, directly or indirectly, in Canada or to or for the account of any resident of Canada in contravention of the securities laws of any province or territory.

The new notes may not be offered or sold in or into the United Kingdom by means of any document except in circumstances that do not constitute an offer to the public within the meaning of the Public Offers of Securities Regulations 1995. All applicable provisions of the Financial Services and Markets Act 2000 must be complied with in respect of anything done in relation to the new notes in, from or otherwise involving or having an effect in, the United Kingdom.

The Mexican National Banking and Securities Commission (*Comisión Nacional Bancaria y de Valores*) will be notified of the terms of the offer for information purposes only, and such notification does not imply a certification as to the investment quality of the new notes, our solvency, liquidity or credit quality, or the accuracy or completeness of the information included in this offering circular. The new notes may not be publicly offered or sold in Mexico and this offering circular may not be publicly distributed in Mexico.

This offering circular does not constitute an offer to sell or a solicitation of an offer to buy the new notes to any person in any jurisdiction where it is unlawful to make such an offer or solicitation.

## **NOTICE TO NEW HAMPSHIRE RESIDENTS**

**NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENSE HAS BEEN FILED UNDER CHAPTER 421-B OF THE NEW HAMPSHIRE REVISED STATUTES WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE OF NEW HAMPSHIRE THAT ANY DOCUMENT FILED UNDER RSA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER, OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.**

## **NOTICE TO PROSPECTIVE INVESTORS IN THE UNITED KINGDOM**

This document is only being distributed to and is only directed at (i) persons who are outside the United Kingdom or (ii) to investment professionals falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the “Order”) or (iii) high net worth entities, and other persons to whom it may lawfully be communicated, falling within Article 49(2)(a) to (d) of the Order (all such persons together being referred to as “relevant persons”). The new notes are only available to, and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such new notes will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely on this document or any of its contents.

## **NOTICE TO PROSPECTIVE INVESTORS IN THE EEA**

To the extent that the offer of the new notes is made in any European Economic Area (“EEA”) member state that has implemented Directive 2003/71/EC (together with any applicable implementing measures in any member state, the “Prospectus Directive”) before the date of publication of a prospectus in relation to the new notes which has been approved by the competent authority in that member state in accordance with the Prospectus Directive (or, where appropriate, published in accordance with the Prospectus Directive and notified

to the competent authority in that member state in accordance with the Prospectus Directive), the offer (including any offer pursuant to this document) is only addressed to qualified investors in that member state within the meaning of the Prospectus Directive or has been or will be made otherwise in circumstances that do not require the issuer to publish a prospectus pursuant to the Prospectus Directive.

## **INDUSTRY AND MARKET DATA**

We obtained the market and certain other data used in this offering circular from our own research, surveys or studies conducted by third parties and industry or general publications, such as Pyramid Research (an Economist Intelligence unit subsidiary) and other publicly available sources. Industry and general publications and surveys generally state that they have obtained information from sources believed to be reliable, but do not guarantee the accuracy and completeness of such information. While we believe that each of these studies and publications is reliable, neither we nor the initial purchasers have independently verified such data, and neither we nor the initial purchasers make any representations as to the accuracy of such information. Certain market share data is based on published information available for the Mexican states. There is no comparable data available relating to the particular cities we serve. In presenting market share estimates for the cities, therefore, we have estimated the size of the market on the basis of the published information for the state in which the particular city is located. We believe this method is reasonable, but the results have not been verified by any independent source.

## **FORWARD-LOOKING STATEMENTS**

Many statements under the captions “Summary,” “Risk Factors,” “Use of Proceeds,” “Management’s Discussion and Analysis of Financial Condition and Results of Operations of Axtel,” “Business” and elsewhere in this offering circular are “forward-looking statements.” These forward-looking statements include, but are not limited to, statements about our plans, objectives, expectations and intentions and other statements contained in the offering circular that are not historical facts. When used in this offering circular, the words “expects,” “anticipates,” “intends,” “plans,” “believes,” “seeks,” “estimates” and similar expressions are generally intended to identify forward-looking statements.

These forward-looking statements reflect our best assessment at the time and thus involve uncertainty and risk. Therefore, these forward-looking statements are qualified by reference to the cautionary statements set forth in this offering circular. It is possible that our future financial performance may differ materially from our expectations due to a variety of factors, some of which include, without limitation, the following:

- competition in local, long distance, data, internet, voice over internet protocol, or VoIP, services and video;
- ability to attract subscribers;
- changes and developments in technology, including our ability to upgrade our networks to remain competitive and our ability to anticipate and react to frequent and significant technological changes;
- our ability to successfully maintain the benefits from the integration of Avantel into Axtel;
- our ability to continue improving the functionality of our WiMax network;
- our ability to manage, implement and monitor billing and operational support systems;
- an increase in churn, or subscriber cancellations;
- the control that certain of our stockholders retain over us;
- changes in capital availability or cost, including interest rate or foreign currency exchange rate fluctuations;

- our ability to service our debt;
- limitations on our access to sources of financing on competitive terms;
- our need for substantial funding sources;
- the effects of governmental regulation of the Mexican telecommunications industry;
- declining rates for long distance traffic;
- changes in the applicable fixed-to-mobile and long-distance termination rates, including legal challenges that could materially delay or completely cancel any benefits arising from new authorities' resolutions;
- fluctuations in labor costs;
- foreign currency exchange fluctuations relative to the U.S. dollar or the Mexican Peso;
- the general political, economic and competitive conditions in markets and countries where we have operations, including competitive pricing pressures, inflation or deflation and changes in tax rates;
- significant economic or political developments in Mexico and the United States;
- the difficult economic and financial situation globally and in Mexico that could significantly reduce demand for our products and services;
- the global telecommunications downturn;
- the timing and occurrence of events which are beyond our control; and
- other factors described in this offering circular.

Any forward-looking statements in this offering circular are based on certain assumptions and analysis made by us in light of our experience and perception of historical trends, current conditions, expected future developments and other factors we believe are appropriate under the current circumstances. Forward-looking statements are not a guarantee of future performance and actual results or developments may differ materially from expectations. You are therefore cautioned not to place undue reliance on such forward-looking statements. While we continually review trends and uncertainties affecting our results of operations and financial condition, we do not intend to update any particular forward-looking statements contained in this document.

### **AVAILABLE INFORMATION**

To permit compliance with Rule 144A under the Securities Act in connection with resales of the notes, we will be required under the indenture under which the notes are issued, upon the request of a holder of Rule 144A notes or Regulation S notes (during the restricted period, as defined in the legend included under "Notice to Investors"), to furnish to such holder and any prospective purchaser designated by such holder the information required to be delivered under Rule 144A(d)(4) under the Securities Act if at the time of the request we are neither a reporting company under Section 13 or Section 15(d) of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act"), nor exempt from reporting pursuant to Rule 12g3-2(b) under the Exchange Act. As long as we maintain this exemption, we will not be required under the indenture to deliver information otherwise required to be delivered under Rule 144A(d)(4) under the Securities Act.

The indenture further requires that we furnish to the Trustee (as defined herein) and the holders of the notes reports and communications that are generally made available to holders of the notes. See "Description of Notes."

We will make available to the holders of the notes, at the corporate trust office of the Trustee at no cost, copies of the indenture as well as this offering circular, including a review of our operations, and annual audited consolidated financial statements prepared in conformity with Mexican Financial Reporting Standards, which we refer to as "Mexican FRS." Information will also be available at the office of the Luxembourg Listing Agent (as defined herein).



We have applied to list the notes on the Official List of the Luxembourg Stock Exchange and for trading on the Euro MTF market. We will be required to comply with any undertakings given by us from time to time to the Luxembourg Stock Exchange in connection with the new notes, and to furnish to them all such information as the rules of the Luxembourg Stock Exchange may require in connection with the listings of the new notes.

Our corporate offices are located at Blvd. Gustavo Díaz Ordaz km. 3.33 No. L-1, Col. Unidad San Pedro, San Pedro Garza García, N.L., Mexico, CP 66215 (Telephone +52(81) 8114-0000). Our website address is [www.axtel.com.mx](http://www.axtel.com.mx). The information on our website is not part of this offering circular.

## **PRESENTATION OF FINANCIAL AND OTHER INFORMATION**

Our financial statements have been prepared in accordance with Mexican FRS. These principles differ in certain respects from U.S. generally accepted accounting principles, which we refer to as “U.S. GAAP.” Differences include, but are not limited to, the treatment of the capitalization of pre-operating expenses, the capitalization of interest, severance, deferred income taxes and employees’ statutory profit sharing and in the presentation of cash flow information. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations of Axtel—Summary of Differences between Mexican FRS and U.S. GAAP.”

The following financial statements are included elsewhere in this offering circular: the audited consolidated financial statements of Axtel, S.A.B. de C.V. and subsidiaries as of December 31, 2009 and 2008 and for the years ended December 31, 2009, 2008 and 2007.

The consolidated financial statements include the assets, liabilities, equity and results on operations of the subsidiaries listed below. The balances and transactions between companies have been eliminated in the preparation of the consolidated financial statements.

We own, directly or indirectly, 100% of the following subsidiaries:

- Avantel Infraestructura, S. de R.L. de C.V. (“Avantel Infraestructura”),
- Avantel, S. de R.L. de C.V. (“Avantel Concesionaria”),
- Instalaciones y Contrataciones, S.A. de C.V. (“Icosa”),
- Servicios Axtel, S.A. de C.V. (“Servicios Axtel”) and
- Telecom Networks Inc. (“Telecom Networks”).

On June 30, 2005, Avantel Infraestructura and certain subsidiaries as partners, together with Avantel Concesionaria, as a representative partner, entered into a joint venture agreement to permit Avantel Concesionaria to provide services and operate Avantel Infraestructura’s public telecommunications network. Under this agreement, Avantel Infraestructura contributed the concessioned network, and the other partners contributed the customer agreements, as well as support and human resources services. As a result of the above, Avantel Infraestructura entered into an agreement with Avantel Concesionaria to transfer the concession rights granted by the Secretaría de Comunicaciones y Transportes (“SCT”).

As a result of the adoption of a new Mexican FRS B-10, commencing January 1, 2008, we no longer use inflation accounting unless the economic environment in which we operate qualifies as “inflationary”, as defined by Mexican FRS (accumulated inflation equal to or higher than 26% in the three preceding years). Because the economic environment in the three-year period ended December 31, 2009 did not qualify as inflationary, we did



not use inflation accounting to prepare our consolidated financial statement as of December 31, 2009. Therefore, financial information as of December 31, 2007 and prior periods is presented in pesos of purchasing power as of December 31, 2007, and financial information beginning January 1, 2008, and for later periods, is presented in nominal pesos pursuant to FRS B-10 “Inflationary Effects.” See Note 3(b) and (o) and Note 4(e) to our audited consolidated financial statements for further information regarding the change with respect to inflationary accounting under Mexican FRS. The figures in our audited financial statements for the years ended December 31, 2009 and 2008 and the year ended December 31, 2007 are not directly comparable given this change to our accounting practices.

When reporting under Mexican FRS and in accordance with FRS B-10, we are required to quantify all financial effects of operating and financing the business under inflationary conditions. For presentation purposes, “comprehensive financing results” refers to the consolidated combined financial effects of:

- net interest expense or interest income;
- changes in the fair market value of financial instruments;
- net gains or losses on monetary position; and
- net foreign exchange gains or losses.

In the financial information included for year 2007, the gain or loss on monetary position refers to gains or losses realized from holding net monetary assets or liabilities and reflect the impact of inflation on monetary assets and liabilities. For example, a gain in monetary position results from holding net monetary liabilities in pesos during periods of inflation, as the purchasing power of the peso declines over time.

Net foreign exchange gains or losses reflect the impact of changes in foreign exchange rates on assets and liabilities denominated in currencies other than pesos. A foreign exchange loss arises if a liability is denominated in a foreign currency which appreciates relative to the peso between the time the liability is incurred and the date it is repaid, as the appreciation of the foreign currency results in an increase in the amount of pesos which must be exchanged to repay the specified amount of the foreign currency liability.

The U.S. dollar amounts provided in this offering circular are translated from the peso amounts, solely for the convenience of the reader, at the exchange rate reported by Mexico’s Central Bank (“Banco de Mexico”) on December 31, 2009 at its noon buying rate for pesos. However, where peso denominated data is given “in nominal pesos,” the amounts provided are pesos actually paid at the time of the expenditure. On December 31, 2009, the noon buying rate for pesos was Ps. 13.0587 per U.S. dollar. These translations should not be construed as representations that the peso amounts represent such U.S. dollar amounts or could be converted into U.S. dollars at the rate indicated as of any dates mentioned in this offering circular.

Sums presented in this offering circular may not add due to rounding.

## **SERVICE OF PROCESS AND ENFORCEMENT OF CIVIL LIABILITIES**

We and our subsidiaries (except for Telecom Networks, Inc., a subsidiary organized in the United States) are either public variable capital corporations (*sociedades anónimas bursátiles de capital variable*), variable capital corporations (*sociedades anónimas de capital variable*), limited liability companies with variable capital (*sociedades de responsabilidad limitada de capital variable*) or fixed capital corporations (*sociedades anónimas*) organized under the laws of Mexico, and are headquartered, managed and operated outside of the United States (principally in Mexico). Most of our directors and officers reside in Mexico. All or a substantial portion of our assets and the assets of most of our directors and officers are located outside of the United States (principally in Mexico). As a result, it may not be possible for the investors or holders of the new notes to effect service of process outside of Mexico or within the United States upon us or such persons, or to enforce a judgment obtained in the United States against us or them outside of Mexico or in the United States courts that is based on the civil liability provisions under laws of jurisdictions other than Mexico, including the federal and state securities laws or other laws of the United States.

We have been advised by our special Mexican counsel, D&A Morales y Asociados, S.C., that no bilateral treaty is in effect between the United States and Mexico calling for the mutual recognition and enforcement of their respective judgments. The recognition by Mexican courts of a judgment rendered in the United States is usually done under the principle of reciprocity, which means that Mexican courts would reexamine judgments rendered in the United States if such foreign country would reexamine Mexican judgments. Mexican courts may enforce judgments rendered in the United States through a homologation procedure consisting of the review by such Mexican courts of the foreign judgment to ascertain whether certain requirements of due process, reciprocity and public policy have been complied with, without reviewing the merits of the subject matter of the case; *provided* that all federal and state procedural requirements under Mexican law (as the applicable case may be), including laws concerning statute of limitations and expirations, are satisfied; and further *provided* that, among others:

- (1) such judgment is final in the rendering state and obtained in compliance with legal requirements of the jurisdiction of the court rendering such judgment and such judgment is in compliance with the terms set forth in the new notes and all legal requirements as the case may be;
- (2) such judgment is strictly for the payment of a certain sum of money, based on an in personam action (*acción personal*) as opposed to an in rem action (*acción real*);
- (3) the judge or court rendering the judgment is considered to have jurisdiction and is competent to hear and judge on the subject matter of the case in accordance with accepted principals of international law that are compatible and analogous with Mexican laws, and the subject matter of the case was not of the exclusive jurisdiction of Mexican courts;
- (4) service of process in the action has been served personally on the defendant or on a duly appointed process agent;
- (5) such judgment does not contravene Mexican law, public policy of Mexico, international treaties or agreements binding upon Mexico or generally accepted principles of international law;
- (6) the applicable procedure under the laws of México with respect to the enforcement of foreign judgments (including issuance of a rogatory letter (*carta rogatoria*) by the competent authority of such jurisdiction requesting enforcement of such judgment and the certification of such judgment as authentic by the corresponding authorities of such jurisdiction in accordance with the laws thereof) is complied with;
- (7) the courts of such jurisdiction would enforce Mexican judgments as a matter of reciprocity;
- (8) the action in respect of which such judgment is rendered is not the subject matter of a lawsuit or legal proceedings among the same parties that is or are pending before a Mexican court, or was resolved by or conflicts with a definitive judgment previously rendered by a Mexican court that has previously served process or delivered a rogatory letter (*carta rogatoria*) to the competent authorities in accordance with the Mexican law;
- (9) the court that rendered such judgment has jurisdiction over the debtor as recognized by the courts of Mexico and in accordance with its conflict of laws rules; and
- (10) the judgment fulfills all necessary requirements to be considered authentic.

Furthermore, there is doubt as to the enforceability, in actions originated in Mexico, of liabilities based in whole or in part on the United States federal or state securities laws and as to the enforceability of judgments obtained in the United States in actions based in whole or in part on the civil liability provisions of United States federal or state securities laws.

## SUMMARY

*Unless otherwise noted or to the extent the context otherwise requires, the terms “Axtel,” “we,” “the Company,” “our Company,” “us” and “our” refer to Axtel, S.A.B. de C.V. and its subsidiaries, and “Avantel” collectively refers to Avantel, S. de R.L. de C.V., Avantel Infraestructura, S. de R.L. de C.V. and their respective subsidiaries. The following summary contains basic information about us and this offering. It likely does not contain all the information that is important to you in making a decision to purchase the new notes. For a more complete understanding of this offering, we encourage you to read this entire offering circular.*

### Our Company

We are the second-largest, and one of the fastest growing, fixed-line, integrated telecommunications companies in Mexico, measured in revenues, EBITDA and lines in service. We offer a wide array of services, including local and long distance telephony, broadband Internet, data and built-to-suit communications solutions in 39 cities and long distance telephone in close to 200 cities to more than 827,000 business and residential customers. In 2009, we generated revenues and operating income of Ps. 10,968.9 million (US\$840.0 million) and Ps. 772.8 million (US\$59.2 million), respectively.

We provide services using a hybrid wireline and fixed wireless local access network (including 1,562 kilometers of metro fiber optic rings) along with approximately 7,700 kilometers of long-haul fiber-optic network. As of December 31, 2009, our last-mile access, designed to optimize capital expenditures through the deployment of network access equipment based on specific customer requirements, includes 57 digital switches, 433 proximity access sites, 155 symmetry access sites, 573 WiMAX access sites, 254 point-to-multipoint sites and 3,103 point-to-point links. Our nationwide long-haul network includes approximately 7,700 kilometers of fiber optic network with links to terminate long distance traffic in close to 200 cities as of December 31, 2009. As of December 31, 2009 we have invested in the aggregate approximately Ps. 29,074.3 million in network and infrastructure.

Our strategy is to continue to penetrate our existing markets by offering a comprehensive portfolio of high quality, facilities-based voice, data, internet, integrated solutions and value-added communications services and to cost-effectively enter into selective new markets with high growth and revenue opportunity. Our approach is to bundle multiple voice, data and Internet services into integrated telecommunications solutions for businesses and high-usage residential customers. We also intend to continue servicing foreign carriers with international traffic termination, as well as providing custom-made integrated telecommunications services to large corporate customers. For the year ended December 31, 2009, approximately 79% of our revenues were generated from business customers and 21% from residential customers.

Axtel was founded in 1994 and in June 1996 was awarded by the Mexican government a concession to install and operate a public telecommunications network for the offering of local and long distance telephony services in Mexico. On December 4, 2006, Axtel acquired Avantel, adding an IP-based nationwide telecommunications network. Due to the acquisition, we now hold the following spectrum assets: two concessions at 929 MHz for radio-messaging services, 56 MHz at 7 GHz for nationwide long-haul point to point transport, 60 MHz at 10.5 GHz in three regions and 60 MHz at 10.5 GHz nationwide for point to multi-point access; 168 MHz at 15 GHz, 368 MHz at 23 GHz for nationwide point to point transport and 112 MHz at 37 to 38.6 GHz in five regions.

We provide local, long distance, data, internet, integrated solutions and value-added communications services in 39 of the largest metropolitan areas in the country, including Mexico City, Monterrey, Guadalajara, Puebla, Toluca, León, Querétaro, San Luis Potosí, Saltillo, Aguascalientes, Ciudad Juárez, Tijuana, Torreón

(Laguna Region), Veracruz, Chihuahua, Celaya, Irapuato, Cd. Victoria, Reynosa, Tampico, Cuernavaca, Merida, Morelia, Pachuca, Hermosillo, San Juan del Rio, Xalapa, Durango, Villahermosa, Acapulco, Mexicali, Cancun, Zacatecas, Matamoros, Nuevo Laredo, Culiacan, Mazatlan, Coahuila and Minatitlán. These 39 cities represent 46.4% of the total population of Mexico according to Mexico's *Instituto Nacional de Estadística Geografía e Informática* or INEGI (Mexican government office in charge of statistics concerning populations, census, agriculture, manufacturing and many other industries). We estimate that our total lines represent approximately 9.7% of the lines in service of our total addressable market in the 39 cities in which we provide local services.

Additionally, our long-haul network provides long distance and data services in close to 200 cities across the country. We expect our growth will come from both continued acquisitions of customers and the build out of our network within our current markets and in selected new cities as we continue to expand our coverage and capacity in the major metropolitan areas of Mexico.

### **The Mexican Telecommunications Industry**

The Mexican telecommunications market is the second largest in Latin America. According to Pyramid Research, revenues from telephony communications services in Mexico, including both fixed and mobile, are expected to grow at a 4.6% compound annual growth rate, from US\$27 billion in 2008 to US\$32 billion in 2012. We believe the following factors will continue to drive the growth in the Mexican telecommunications market:

*Market Size and Projected Growth Trends.* Mexico is the second largest country in Latin America in terms of population, with approximately 107 million people as of December 31, 2009, and a gross domestic product of US\$1,088.1 billion and a gross domestic product per capita of US\$10,177 as of December 31, 2008. According to Pyramid Research, Mexico has relatively low wireline penetration compared to other countries in Latin America; with 18.3 lines per 100 inhabitants at the end of 2008. This penetration is expected to remain stable until 2012 with some participants losing market share while others, mostly competitive local exchange carriers, gain or increase market share. The fixed communications sector, which includes basic telephony, such as local and long distance voice services, and data telecommunications services, such as internet and private virtual networks, is an important part of the Mexican telecommunications industry because of its size and growth opportunity. In 2009, revenues from the fixed communications sector were approximately US\$10.2 billion.

*Favorable Regulatory Environment.* The Mexican telecommunications market has long been dominated by Teléfonos de Mexico, S.A.B. de C.V. ("Telmex"), the former government-owned telecommunications monopoly. Since the Mexican government completed the privatization of Telmex in 1990, the Mexican telecommunications sector has become increasingly open to competition. The opening of the Mexican telecommunications market has created an opportunity for competitive carriers to capture market share from Telmex. As the owner and operator of a network servicing Mexico's largest metropolitan markets, we believe we are well positioned to continue to take advantage of this market opportunity.

### **Competitive Strengths**

*Leading Market Position.* As one of the first competitive providers to approach customers with bundled local, long distance voice and data services in a significant number of cities across the country, we believe that we are able to meet pent-up demand for an alternative service provider and establish brand awareness and customer relationships prior to market entry by emerging competitors. We have benefited from our "first-competitor-to-market" advantage by capturing what we estimate to be approximately a 9.7% share of our total addressable market in the 39 cities where we offer local services as of December 31, 2009. In Monterrey and Guadalajara, the first two markets where Axtel launched operations in 1999, we estimate that as of December 31, 2009 we have a market share of approximately 15% and 13%, respectively.

*Comprehensive Voice and Data Service Portfolio.* We provide our customers an integrated bundle of services that includes local and long distance voice services, as well as internet, data and other value-added services. We believe our comprehensive service portfolio enables us to build strong, long-term relationships with customers and increase our return on our investment in network infrastructure. Furthermore, our digital access, transport and innovative last-mile technologies enable us to meet the growing demand for data services.

*Scalable Digital Network.* Our hybrid fixed wireless and wireline local access network structure allows us to enter new markets quickly and cost-effectively. By utilizing the fixed wireless access technology model, we are able to quickly cover a substantial geographic area with reduced initial capital expenditures. We defer most incremental capital expenditures for last-mile connectivity until the customer subscribes to our service. As of December 31, 2009, our network consisted of 57 digital switches, 433 Proximity access sites, 155 Symmetry access sites, 573 WiMAX access sites, 254 point-to-multipoint sites, 3,103 point-to-point links and 1,562 kilometers of metropolitan fiber optic rings. As of December 31, 2009, we have invested in the aggregate approximately Ps. 29,074.3 million in network and infrastructure to build an extensive local and national telecommunications network.

*Flexible and Innovative Technology.* Our ability to add new last-mile technologies allows us to continuously satisfy the changing requirements of existing and new customers. The deployment of 802.16e WiMAX, a new IP-based voice and data wireless technology designed to deliver voice and data solutions, under fixed, portable, nomadic and mobile environments, increases our ability to provide high-quality voice and data access solutions. We have initiated the gradual conversion of selected coverage clusters from wireless technologies to fiber. Such conversion will enhance our ability to provide integrated data, voice and video services. The conversion criteria are based on existing customer density and potential business opportunities. A significant portion of the existing wireless technologies can be re-deployed to other areas.

*Scale—Second-Largest Fixed-Line Integrated Telecommunications Company in Mexico.* We are the second largest local, national and international long distance and data services provider in Mexico, measured in lines in service, revenues and EBITDA. The size of our operations enables us to benefit from economies of scale.

*Favorable Financial Profile.* We have favorable Adjusted EBITDA generation (Ps. 3,838.6 million in 2009 and Ps. 4,075.3 million in 2008) and financial ratios with net debt to Adjusted EBITDA of 2.3x and 2.1x for each of the years ended on December 31, 2009 and December 31, 2008, respectively, and Adjusted EBITDA to net interest expense of 4.8x for the year ended December 31, 2009, excluding the premium paid for the tender offer and early redemption of the 2013 senior notes, and 5.1x for the year ended December 31, 2008. See “Selected Financial Data.”

*Experienced Management Team and Internationally Renowned Equity Partners.* Our senior management team has extensive entrepreneurial, financial, marketing and telecommunications expertise. The diverse experience of our senior management team has contributed significantly to our initial success and rapid growth. In addition, we have benefited from working currently and in the past with strong local partners and experienced multinational investors such as The Blackstone Group, Citigroup Inc. and AIG-GE’s Latin American Infrastructure Fund. Our local investors and directors include, among others, Tomás Milmo Santos, Thomas Milmo Zambrano, Alberto Santos de Hoyos, Lorenzo Zambrano Treviño and senior executives from Banco Nacional de México S.A., Institución de Banca Múltiple, Grupo Financiero Banamex (“Banamex”). These investors have extensive financial, operating and senior management experience in large Mexican corporations.



## Strategy

The key elements of our business strategy are:

*Target Service Sectors with High Profitability Potential.* We have divided our target market into the business market and residential market. Within the business market, we address the needs of micro and small business as well as medium and large companies, multinationals, financial institutions and government entities. We have developed differentiated, targeted telecommunications services plans designed to capture business and retain high-usage customers in each market. In the residential market, we focus on high-usage customers. We believe that by focusing on the business and high-usage residential customers within a coverage area we are able to increase the return per dollar invested in our network infrastructure. For the year ended December 31, 2009, approximately 79% of our revenues were generated from business customers and 21% from residential customers.

*Bundle Products in an Integrated Offering.* We believe that the bundling of voice, data and internet services into communications solutions for our customers enables us to generate higher revenue per customer and more revenue per dollar invested in access infrastructure while also generating customer loyalty. We have focused and will continue to focus on increasing the penetration of bundled products to our customer base. By being a facilities-based telecommunications service provider, we believe we are well positioned to offer our customers the convenience of receiving voice, data and internet services from a single provider. For corporate customers, financial institutions and government entities, we offer integrated solutions based on the specific needs of the customers, including design, implementation, maintenance and monitoring of their networks. For medium-size clients, we bundle voice and data packages that specifically meet their requirements in a cost-efficient way. For residential clients, we intend to use our DTH concession to combine data and voice services with video solutions, which we believe will provide our residential customers better pricing through bundled voice, data and video services. See “Business—Products and Services.”

*Maintain Voice Revenues Stream.* Although the data market represents an attractive and expanding revenues opportunity compared to slow growing voice-related revenues, over 70% of Mexican telecommunications industry revenues in 2009 are voice related. A significant voice revenue stream provides the leverage to further penetrate the fast-growing data market. Therefore, we will continue to strive to maintain a stable voice revenue stream.

*Focus on Customer Service and Retention.* Since launching operations, we have been focused on achieving customer satisfaction levels that are superior to the incumbent and our primary competitors. We believe that our service-driven customer care leads to superior customer satisfaction, which enhances profitability and cash flow by increasing customer retention and expanding sales opportunities.

*Continue to Expand Technologically Advanced Network Infrastructure.* We continuously evaluate opportunities for network expansion both within our existing cities and additional regions in order to enhance our coverage area. We believe that selectively expanding our network and coverage area will enhance our ability to acquire large business customers with multi-city operations, which we expect will result in higher revenues and margin improvements while minimizing capital expenditures. We may also expand our network or operations through acquisitions or strategic agreements, as we believe there may be additional opportunities for consolidation in the Mexican telecommunications industry. We are not currently engaged in formal negotiations with any company regarding a potential acquisition or strategic agreement but may engage in conversations with third parties from time to time regarding strategic acquisitions or combinations.

### **Recent Developments**

On September 15, 2009, Mexico's Ministry of Communications and Transportation granted us a concession to provide direct-to-home ("DTH"), or satellite-TV, video services in Mexico. As a result of obtaining this concession, we believe Axtel will be able to set up its DTH infrastructure and offer bundled voice, internet and video services, which will enable us to compete more effectively in the residential segment, particularly with triple-play offers from cable companies.

On September 22, 2009, we issued US\$300.0 million of 9.0% Senior Unsecured Notes due 2019 at an issue price of 100% (the "existing notes"). We used the proceeds of the existing notes and cash on hand to (i) to partially prepay our term loan facility due 2012 (the "2012 Term Loan Facility") in a principal amount equal to US\$85 million, (ii) to fund the tender offer for any and all of our outstanding US\$162.5 million in aggregate principal amount 11% senior notes due 2013 (the "2013 Notes") at the tender offer prices, (iii) to redeem the 2013 Notes that remained outstanding after the expiration of the tender offer, (iv) for general corporate purposes, capital investments and working capital requirements.

On October 7, 2009, the Company filed a Form 15F with the SEC terminating its reporting obligations with respect to the 2013 Notes. The termination became effective on January 5, 2010.

The Company is in negotiations to enter into a 3-year revolving credit facility (the "New Revolving Credit Facility") concurrently with or soon after the issuance of the new notes, which will provide for borrowings of up to approximately US\$30 million, subject to customary terms and conditions. Currently, the Company does not have plans to draw on this facility. The Company plans to use this New Revolving Credit Facility as a liquidity back-up facility that may be used in the future for general corporate purposes, capital investments and working capital requirements. The closing of the new revolving credit facility will be subject to customary closing conditions. The offering of the new notes is not conditioned upon our entering into the New Revolving Credit Facility.

### **Corporate Information**

Our corporate offices are located at Blvd. Gustavo Díaz Ordaz km. 3.33 No. L-1, Col. Unidad San Pedro, San Pedro Garza García, N.L., Mexico, CP 66215 (Telephone +52(81) 8114-0000). Our website address is [www.axtel.com.mx](http://www.axtel.com.mx). The information on our website is not part of this offering circular.



## The Offering

*The summary below describes the principal terms of the new notes. Some of the terms and conditions described below are subject to important limitations and exceptions. "Description of the Notes" beginning on page 96 contains a more detailed description of the terms and conditions of the new notes.*

Issuer .....	Axtel, S.A.B. de C.V.
Securities Offered .....	US\$190,000,000 in aggregate principal amount of 9.0% Senior Unsecured Notes due 2019. The new notes are being offered as additional debt securities under the indenture dated September 22, 2009, pursuant to which we have previously issued US\$300.0 million aggregate principal amount of 9.0% Senior Unsecured Notes due 2019. The new notes will be treated as a single series with the existing notes and will have the same terms as those of the existing notes. The new notes and the existing notes will vote as one class under the indenture governing the notes. Immediately after giving effect to the issuance of the new notes offered by this offering circular, we will have US\$490.0 million aggregate principal amount of our 9.00% Senior Unsecured Notes due 2019. Unless otherwise expressly stated or the context otherwise requires, references in this offering circular to our "9.0% Senior Unsecured Notes due 2019" and the "notes" include both the new notes offered hereby and the existing notes.
Maturity Date .....	September 22, 2019.
Guarantees .....	Except for Telecom Networks Inc., each of our current subsidiaries and certain of our future subsidiaries will guarantee the new notes with unconditional guarantees that will be unsecured. From and after the issue date, subject to certain exceptions, each subsidiary that guarantees any of our indebtedness will be required to guarantee the new notes on the same basis. See "Description of the Notes—Guarantees."
Interest Payments .....	Interest on new notes will be payable semi-annually in arrears on March 22 and September 22 of each year, commencing September 22, 2010. Interest will accrue from March 22, 2010.
Ranking .....	The new notes, together with the existing notes, are our senior unsecured obligations. Accordingly, the new notes will rank: <ul style="list-style-type: none"><li>• effectively junior in right of payment to all existing and future secured indebtedness, to the extent of the collateral securing that indebtedness and indebtedness owed to statutorily preferred creditors;</li><li>• equal in right of payment to any of our existing and future senior unsecured indebtedness, including our existing notes, and will be treated as one series with such existing notes for all purposes under the indenture governing the new notes; and</li></ul>

- senior in right of payment to any of our existing and future subordinated indebtedness.

In addition, the guarantees of the notes by our subsidiaries that guarantee any of our indebtedness will rank equally to all of such subsidiaries' existing and future senior unsecured obligations including indebtedness arising under the guarantees of our existing notes. The notes and the guarantees thereof will be effectively subordinated to all secured indebtedness of the guarantors to the extent of the assets securing such indebtedness and indebtedness owed to statutorily preferred creditors.

As of December 31, 2009, after giving effect to the Refinancings and the issuance of the new notes and our use of proceeds therefrom, we would have had approximately US\$842.8 million of outstanding debt (including the new notes) and accrued interest net of derivative instruments and (excluding intercompany liabilities and guarantees) and the notes and guarantees would have ranked effectively junior in right of payment to approximately US\$12.0 million of secured liabilities.

Optional Redemption . . . . . Prior to September 22, 2014 we may redeem some or all of the notes at a redemption price equal to 100.0% of the principal amount, plus accrued and unpaid interest, if any, plus a “make whole” premium as described in this offering circular. We may redeem any of the notes at any time on or after September 22, 2014 in whole or in part, in cash, at the redemption prices described in this offering circular, plus accrued and unpaid interest to the date of redemption.

At any time prior to September 22, 2012 we may redeem up to 35% of the aggregate principal amount of the notes issued under the indenture with the net proceeds of certain equity offerings at a redemption price equal to 109% of the principal amount of the notes plus accrued and unpaid interest to the date of redemption. We may make that redemption only if, after the redemption, at least 65% of the aggregate principal amount of notes issued under the indenture remains outstanding.

Additional Amounts . . . . . Subject to certain exceptions, we will pay Additional Amounts (as defined under “Description of the Notes—Additional Amounts”) so that the net amount received by each holder of notes after the payment of certain withholding taxes will be equal to the amount that would have been received by each such holder if no such withholding tax had been payable.

Redemption for Tax Reasons . . . . . Under certain circumstances, we may redeem the notes in whole but not in part upon not less than 30 and no more than 60 days prior notice at a price equal to 100% of the principal amount thereof, together with accrued and unpaid interest to the date fixed for redemption plus any additional amounts. See “Description of the Notes—Redemption for Changes in Withholding Taxes.”

Change of Control .....	If we experience a Change of Control (as defined under “Description of the Notes—Change of Control”), we will be required to make an offer to repurchase the notes at a price equal to 101% of the principal amount thereof, plus accrued and unpaid interest to the date of repurchase.
Certain Covenants .....	<p>The terms of the notes will restrict our ability and the ability of our restricted subsidiaries to, among other things:</p> <ul style="list-style-type: none"> <li>• incur additional indebtedness or issue preferred stock;</li> <li>• pay dividends or make other distributions to our stockholders;</li> <li>• purchase or redeem capital stock or subordinated indebtedness;</li> <li>• make investments;</li> <li>• create liens;</li> <li>• incur restrictions on the ability of our restricted subsidiaries to pay dividends or make other payments to us;</li> <li>• sell assets;</li> <li>• consolidate or merge with or into other companies or transfer all or substantially all of our assets; and</li> <li>• engage in transactions with affiliates.</li> </ul> <p>These limitations will be subject to a number of important qualifications and exceptions. See “Description of the Notes—Certain Covenants.”</p>
Transfer Restrictions .....	The issuance of the new notes has not been registered under the Securities Act and may not be offered or sold, except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. See “Transfer Restrictions.”
No Prior Market .....	The new notes will be new securities for which there is no market. Although the initial purchasers have informed us that they intend to make a market in the new notes they are not obligated to do so and may discontinue market-making at any time without notice. Accordingly, we cannot assure you that a liquid market for the new notes will develop or be maintained.
Listings .....	We have applied to list the notes on the Official List of the Luxembourg Stock Exchange and for trading on the Euro MTF market. We cannot assure investors, however, that this application will be accepted.
No Registration Rights .....	We are not required to register the new notes for resale under the Securities Act, or the securities laws of any other jurisdiction, and are not required to offer to exchange the new notes for new notes registered under the Securities Act or the laws of any other jurisdiction.

Use of Proceeds ..... We intend to use the net proceeds from this offering of new notes, which are estimated to be approximately US\$192.6 million after deducting estimated underwriting discounts and offering expenses, (i) to prepay US\$105 million of the aggregate principal amount of indebtedness outstanding under our 2012 Term Loan Facility, (ii) to repay approximately US\$32 million of our short-term indebtedness under the Banamex Promissory Note, (iii) to fund approximately US\$30 million of principal installments on our indebtedness that will become due during 2010, and (iv) for general corporate purposes, capital investments and working capital requirements. See “Description of Other Indebtedness.”

CUSIP Numbers ..... The new notes offered and sold in offshore transactions in reliance on Regulation S will be issued under a temporary CUSIP number to be used during the distribution compliance period pursuant to Regulation S.

### **Risk Factors**

Investing in the new notes involves substantial risks. See “Risk Factors” for a discussion of certain factors you should consider in evaluating an investment in the new notes.

### **Summary Consolidated Historical Financial Information**

We derived the following summary historical consolidated financial data as of December 31, 2009, 2008 and 2007 (other than balance sheet data for the 2007 fiscal year) and for the three years ended December 31, 2009, 2008 and 2007 from Axtel's audited consolidated financial statements included elsewhere in this offering circular.

You should read the information presented below in conjunction with "Use of Proceeds," "Capitalization," "Management's Discussion and Analysis of Financial Condition and Results of Operations of Axtel" and the consolidated financial statements and the new notes thereto included elsewhere in this offering circular.

Our consolidated financial statements have been prepared in accordance with Mexican FRS. These standards differ in certain respects from U.S. GAAP, including, but not limited to, the treatment of the capitalization of pre-operating expenses, the capitalization of interest, severance, and deferred income taxes and employees' statutory profit sharing and in the presentation of cash flow information. See "Management's Discussion and Analysis of Financial Condition and Results of Operations of Axtel—Summary of Differences between Mexican FRS and U.S. GAAP."

The figures in our audited consolidated financial statements for the years ended December 31, 2009 and 2008 and the year ended December 31, 2007 are not directly comparable due to the Company stopped recognizing inflationary effects beginning on January 1, 2008, pursuant to FRS B-10 "Inflationary Effects." See Note 3(b) and (o) and Note 4(e) to our audited consolidated financial statements for further information regarding the change with respect to inflationary accounting under Mexican FRS.

The following tables set forth selected financial data for the periods indicated, stated in nominal pesos for the years ended December 31, 2009 and 2008 and in constant pesos as of December 31, 2007 for the year ended December 31, 2007. The convenience translation exchange rate is Ps. 13.0587 per U.S. dollar.

	Year Ended December 31,			Unaudited Convenience Translation
	2007	2008	2009	Year Ended December 31, 2009
	(Millions of Ps.)			(Millions of US\$)
<b>Statement of Income Data:</b>				
Telephone services and related revenues . . . .	Ps. 12,190.6	Ps. 11,572.4	Ps. 10,968.9	US\$ 840.0
Cost of revenues and operating expenses . . . .	(10,796.8)	(10,217.8)	(10,196.1)	(780.8)
Income from operations . . . . .	1,393.8	1,354.6	772.8	59.2
Interest expense, net . . . . .	(790.6)	(742.7)	(900.7)	(69.0)
Foreign exchange gain (loss), net . . . . .	1.0	(1,602.1)	(279.8)	21.4
Change in the fair value of derivative instruments . . . . .	19.9	54.1	212.3	16.3
Monetary position . . . . .	268.8	—	—	—
Other (expense) income, net. . . . .	(20.1)	(68.4)	1.1	0.1
Income (loss) before income taxes . . . . .	872.8	(1,004.7)	365.3	28.0
Income tax (expense) benefit. . . . .	(383.2)	301.6	(181.4)	(13.9)
Equity in results of associated company . . . .	1.4	2.8	(7.4)	(0.6)
Net income (loss) . . . . .	Ps. 491.0	Ps. (700.3)	Ps. 176.4	US\$ 13.5

	As of December 31,		Unaudited Convenience Translation
	2008	2009	As of December 31, 2009
	(Millions of Ps.)		(Millions of US\$)
<b>Balance Sheet Data:</b>			
Cash and cash equivalents . . . . .	Ps. 1,105.6	Ps. 1,402.2	US\$ 107.4
Capital common stock . . . . .	7,562.1	7,562.1	579.1
Total assets . . . . .	21,569.2	21,603.1	1,654.3
Total debt . . . . .	9,791.1	10,107.7	774.0
Total liabilities . . . . .	13,637.7	13,402.1	1,026.3
Total stockholders' equity . . . . .	7,931.4	8,200.9	628.0
Net Assets(1) . . . . .	14,918.6	15,507.2	1,187.5

(1) "Net Assets" is determined by adding property, systems and equipment, and net working capital investment, which is determined by subtracting from current assets, cash, income tax payable, accounts payable and other accounts payable.

### Adjusted EBITDA Reconciliation of Axtel

EBITDA is defined as net income plus net interest expense, taxes, employee statutory profit sharing, depreciation and amortization. Adjusted EBITDA is not a financial measure computed under Mexican FRS or U.S. GAAP. Adjusted EBITDA is defined as EBITDA adjusted to exclude non-recurring items and other adjustments. Axtel believes that the inclusion of supplementary adjustments to EBITDA applied in presenting Adjusted EBITDA is appropriate to provide additional information to investors about certain material non-cash and non-recurring items. Such adjustments to EBITDA may not be in accordance with current SEC practice or with regulations adopted by the SEC that apply to registration statements filed under the Securities Act and periodic reports filed under the Exchange Act. The following table reconciles EBITDA, as presented above, to net income (loss) and further reconciles Adjusted EBITDA to EBITDA.

	Year Ended December 31,			Unaudited Convenience
	2007	2008	2009	Translation
	(Millions of Ps.)			Year Ended
				December 31, 2009
				(Millions of US\$)
Net income (loss) .....	Ps. 491.0	Ps. (700.3)	Ps. 176.4	US\$ 13.5
Depreciation and Amortization.....	2,690.7	2,855.8	3,065.8	234.8
Interest expense, net .....	790.6	742.7	900.7	69.0
Income tax expense (benefit) .....	383.2	(301.6)	181.4	13.9
EBITDA .....	Ps. 4,355.5	Ps. 2,596.7	Ps. 4,324.4	US\$ 331.1
Foreign exchange (gain) loss, net.....	(1.0)	1,602.1	(279.8)	(21.4)
Monetary position .....	(268.8)	—	—	—
Change in the fair value of derivative instruments.....	(19.9)	(54.1)	(212.3)	(16.3)
Other expense (income), net .....	20.1	68.4	(1.1)	(0.1)
Equity in results of associated company .....	(1.4)	(2.8)	7.4	0.6
Adjustment to bad debt expense from previous years .....	—	(135.1)	—	—
Adjusted EBITDA.....	<u>Ps. 4,084.5</u>	<u>Ps. 4,075.3</u>	<u>Ps. 3,838.6</u>	<u>US\$ 293.9</u>



## RISK FACTORS

*You should carefully consider the following risk factors, as well as other information set forth in this offering circular, prior to making an investment in the new notes. The risks described below are not the only ones that may affect the new notes. Additional risks not presently known to us or that we currently deem immaterial may also impair our business operations. In general, investing in the securities of issuers in emerging-market countries such as Mexico involves risks not typically associated with investing in the securities of U.S. companies. Where the following discussion addresses the Mexican government or Mexican macroeconomic data, the following information is based on information taken from official publications of the Mexican government.*

### **Risks Relating to Our Company**

#### **Our network growth strategy may fail to generate the revenues we anticipate.**

From our inception through December 31, 2009, we have invested approximately Ps. 29,074.3 million in network and infrastructure. We anticipate making significant additional expenditures to maintain and upgrade our network and to expand our network, geographic presence and business for the future. These expenditures, together with operating expenses, may adversely impact our cash flow and profitability, particularly if the expenditures do not lead to additional revenue. We also anticipate that continued growth will require us to attract and retain qualified personnel necessary to efficiently manage such growth. If we are unable to meet the challenges that our growth presents, our results of operations and financial condition could be adversely affected.

#### **We have a history of substantial losses and expect to incur future losses.**

We have incurred a cumulative net loss of Ps. 273.9 million from inception to December 31, 2009. We anticipate that we could continue to incur net losses in the future.

#### **If the decline in revenues and operating income recorded by the Company during 2009 as compared to 2008 were to persist, our financial results and operations would be adversely affected, perhaps materially.**

For each quarter of the fiscal year 2009 the Company recorded a decline in revenues and operating income when compared to the same periods in 2008. Such decrease in revenues and operating income may indicate a continuing downward trend in the financial results of the Company for 2010. Such downward trend is explained in part by our loss of revenue from some of our customers, particularly Nextel de Mexico (“Nextel”), the economic recession that Mexico is undergoing, further penetration of bundled commercial offers, including calls free of charge and our reduction in fixed-to-mobile unit prices resulting from lower fixed-to-mobile costs. If such downward trend were to persist through 2010, our financial results and operations would be adversely affected, perhaps materially.

#### **Our increased leverage resulting from the acquisition of Avantel could significantly affect our growth and operating results.**

We financed the acquisition of Avantel in 2006 with approximately US\$516.0 million in debt. As of December 31, 2009, our total debt and accrued interest, net of derivatives instruments, was Ps. 9,874.1 million, and, after giving effect to this offering and our use of proceeds therefrom, we would have had Ps. 11,005.7 million of outstanding debt and accrued interest, net of derivative instruments (excluding intercompany liabilities and guarantees), a significantly larger amount compared to the pre-Avantel acquisition levels. The resulting increase in debt service costs could reduce the amount of cash which would otherwise be available to invest in the expansion of our business or to meet other obligations. Likewise, our higher level of leverage could reduce our access to new financing sources on favorable terms, and accordingly, significantly limit our growth and adversely affect our operating results.

#### **We depend on certain important customers for a significant portion of our revenues.**

Our three largest customers generated approximately 22% of our total revenues in 2009. Accordingly, our ability to maintain a satisfactory relationship with these customers has a direct impact on our revenues and profitability. If these customers breach some or all the conditions established in their respective commercial

agreements, or such agreements are not renewed upon their respective expiration dates, our business, financial condition, revenues and results of operations could be adversely affected.

One of our largest customers is Nextel de Mexico. We first entered into a services agreement with Nextel de Mexico in April 2001, and this agreement has been extended eight times. Pursuant to this business relationship, we extended the agreement until August 31, 2011 to continue providing Nextel with local services, spectrum, long distance, 1-800 numbers and other services in a significant number of Mexican cities. Under this extension, Nextel will gradually exclude certain Mexican cities by August 31, 2011, and the respective traffic or volume generated by those cities from the agreement every year, thereby reducing Nextel's contribution to our revenues.

**We operate in a highly competitive environment and experience significant rate pressure, which may negatively affect our operating margins.**

The telecommunications industry in Mexico is becoming more competitive. Over the past eight years, we have not increased prices for local and long distance services to our customers. Additionally, in 2006 the government enacted a new legislation and convergence policy, which established the guidelines for the provision of voice, data and video services by telecommunications companies, including bundled services. The new legal framework will facilitate the entrance of new participants into the Mexican telecommunications and data market, such as cable companies, broadcasting companies, and the state-monopoly Federal Electricity Commission (Comisión Federal de Electricidad, or "CFE"). Although it does not currently affect our operations directly, broadcasters such as Grupo Televisa, S.A.B. ("Televisa") and TV Azteca S.A.B. de C.V. ("TV Azteca") and cellular service providers such as América Móvil S.A.B. de C.V. might be allowed to retain excess bandwidth in their networks, and if granted the corresponding concessions or amendments thereto, they will have the capability to provide services similar to those that we currently provide or intend to provide in the near future, including digital channels, internet service and IP telephony. In addition, it is unclear what impact the recent alliance between Televisa and Nextel de Mexico will have on our business. Thus, assuming the related investment is consummated, we cannot assure you that this alliance will not negatively impact our operations or increase competition. We expect the Mexican telecommunications market to continue to experience rate pressure, primarily as a result of:

- increased competition and focus by our competitors on increasing market share;
- recent technological advances that permit substantial increases in the transmission capacity of both new and existing fiber-optic networks, resulting in long distance overcapacity and rate pressure;
- major participation of traditional fixed-line competitors;
- the entrance of cable television operators into certain of our markets; and
- the entrance of new competitors, such as broadcasting companies (Televisa or TV Azteca), or CFE.

As the telecommunications industry in Mexico becomes more competitive, we will face significant competition from other operators, primarily on the basis of features, pricing and customer service. Some of these competitors include Telmex, Alestra, S.A. de C.V. ("Alestra") and Maxcom Telecomunicaciones, S.A.B. de C.V. ("Maxcom"), as well as established local cable television operators who may expand their services into certain of our markets, such as local and long distance voice and data service. As resellers of telephony services become licensed, they will also offer competition in many of our targeted markets. Additionally, should any changes to current foreign investment restrictions applicable to fixed telecommunications networks (*redes fijas de telecomunicaciones*) be adopted such that a higher percentage of foreign investment is permitted, we could face increased competition from new international operators. There can be no assurance that such an increased competitive environment will not affect our business and results of operations.

Telmex, as the former state-owned telecommunications monopoly and dominant provider of local and other telecommunications services in Mexico, has significantly greater financial and other resources than those available to us. In addition, Telmex's nationwide network and concessions, as well as its established and long-standing customer base, give it a substantial competitive advantage over us.

Furthermore, given the concentration, declining prices and reduced margins of the Mexican Telecommunications market, price wars could result if Telmex attempts to maintain its dominant market position. If there are further declines in the price of telecommunication services in Mexico, we will be forced to competitively react to those price declines by lowering our margins or risk losing market share, which would adversely affect our operating results and financial position.

**We depend on certain vendors for the deployment of our network.**

Our ability to achieve our strategic objectives and our overall performance and prospects depends on and will depend on, in large part, the successful, timely and cost-effective acquisition and performance of telecommunications equipment including wireless access products, such as WiMAX-based technology equipment deployed in 2008. If any of our vendors, including Motorola de Mexico S.A. and Motorola Inc., which provided the 802.16e WiMAX technology (“WiMAX” or “Wimax”) for a significant portion of our 2008 and 2009 network access infrastructure investments, are unable or fail to continue supplying products, or if WiMAX is not able to comply with its expected capabilities, our network expansion and growth could be slowed and our operating results could be adversely affected.

**We experienced significant malfunctions in the implementation and service availability of our WiMAX network in 2008.**

Our residential and small and medium-sized enterprises are served using WiMAX-based technology among other technologies. In 2008, we experienced malfunctions in the implementation of our WiMAX network, which consisted of lack of service availability and the inability to provide certain functions of the WiMAX network, adversely affecting the perception of reliability needed to attract customers under this technology. Although, a significant portion of the problems and technology malfunctions have been resolved, new problems might arise again in the future. If further delays occur again in the future or if WiMAX is not able to comply with its expected capabilities, our growth could be slowed and our operating results could be adversely affected.

**Federal tribunals may rescind or nullify SCT’s resolution approving a reduction in tariffs for termination of local calls from Axtel and Avantel to cellular telephone companies, which could have a material adverse effect on our business and results of operations.**

On September 1, 2008, SCT resolved interconnection disputes between the Company and certain cellular telephone companies including, without limitation, Radiomóvil Dipsa, S.A. de C.V. and affiliates (“Telcel”), Iusacell PCS, S.A. de C.V. and affiliates (“Iusacell”), Pegaso PCS, S.A. de C.V. and affiliates (“Telefónica Movil”) and Operadora Unefon, S.A. de C.V. (“Unefon”) regarding tariffs for termination of local calls from the Company to such cellular telephone companies. In the administrative resolutions, SCT approved a reduction in the tariffs for termination of local calls from Axtel to cellular telephone companies. These tariffs were reduced from Ps. 1.32 for each real minute to Telcel and Ps. 1.21 for each rounded minute to the other cellular telephone companies (Iusacell, Telefónica Movil and Unefon) to Ps. 0.5465 per minute to Telcel and Ps. 0.6032 per minute to the other cellular telephone companies. See “Business– Regulatory Proceedings.”

Pursuant to the SCT’s resolutions, the Company and Avantel started applying the new interconnection fees in August 2008. Nevertheless, all cellular telephone companies continued to invoice the Company and Avantel for traffic termination under the “Calling Party Pays” model applying the interconnection fees in effect prior to the SCT resolutions. As of December 31, 2009, the difference between the amounts paid by the Company and Avantel according to the new rates and the amounts invoiced by the cellular telephone companies amounted to approximately Ps. 950.0 million before Value Added Tax, for which we have not established a reserve.

Telcel and other cellular telephone companies have challenged the validity of the SCT’s resolutions before the *Juzgados de Distrito* (the “Federal Courts”). We cannot assure you that the courts will not rule against us by declaring the SCT’s resolutions null and void, increasing the rates we have to pay to cellular telephone

companies going forward, and possibly giving retroactive application to the tariffs paid by Axtel and Avantel prior to the SCT resolutions, thereby obligating us to pay the cellular telephone companies their invoiced and unpaid amounts. An adverse ruling from the Federal Courts could have a material adverse effect on our business and results of operations.

**We depend on key personnel; if they were to leave us, we might have an insufficient number of qualified employees.**

We believe that our ability to implement our business strategy and our future success depends on the continuous employment of our senior management team, in particular our president and chief executive officer, Tomás Milmo Santos. Our senior management team has extensive experience in the industry and is vital in maintaining some of our major customer relationships, which might be difficult to replace. The loss of the technical knowledge, management and industry expertise of these key employees could make it difficult for us to execute our business plan effectively and could result in delays in new products being developed, loss of customers and diversion of resources while we seek replacements.

**If we do not successfully maintain, upgrade and efficiently operate accounting, billing, customer service and management information systems, we may not be able to maintain and improve our operating efficiencies.**

Sophisticated information and processing systems are vital to our operations and growth and our ability to monitor costs, render monthly invoices for services, process customer orders, provide customer service and achieve operating efficiencies. We have installed the accounting, information and processing systems that we deem necessary to provide services efficiently. However, there can be no assurance that we will be able to successfully operate and upgrade such systems or complete the migration of some pending elements from Avantel's former operations onto such systems or that these systems will continue to perform as expected. Any failure in our information and processing systems could impair our ability to collect payment from customers and respond satisfactorily to customer needs.

**Our operations are dependent upon our ability to protect our network infrastructure.**

Our operations are dependent upon our ability to protect our network infrastructure against damage from fire, earthquakes, hurricanes, floods, power loss, breaches of security, software defects and similar events and to construct networks that are not vulnerable to the effects of such events. The occurrence of a natural disaster or other unanticipated problems at our facilities or at the sites of our switches could cause interruptions in the services we provide. The failure of a switch would result in the interruption of service to the customers served by that switch until necessary repairs were made or replacement equipment was installed. Repairing or replacing damaged equipment may be costly. Any damage or failure that causes interruptions in our operations could have a material adverse effect on our business, financial condition and results of operations.

**We depend on Telmex for interconnection and we may be forced to pay higher interconnection fees in the future, which could have a material adverse effect on our business and results of operations.**

Telmex exerts significant influence on all aspects of the telecommunications markets in Mexico, including interconnection agreements. We use Telmex's network to terminate the vast majority of our customers' calls. The interconnection agreement between Axtel and Telmex expired on December 31, 2008. The contract contains provisions for its continuous application; if the agreement expires without having been expressly extended by the parties, the agreement explicitly contemplates an automatic extension until both parties mutually agree to extend the expired agreement or execute a new interconnection agreement. During 2006 and 2007, the contract had expired and Axtel and Telmex interconnected with each other pursuant to the continuous application of the provisions of the contract until March 2008 at which time an extension was signed. However, if Telmex breaches some or all the conditions established in the interconnection agreement, or if we are not able to renew this agreement under acceptable terms following its expiration, we might be forced to offer services that will no

longer be profitable and competitive. In addition, if the SCT or the Mexican telecommunications regulatory authority (*Comisión Federal de Telecomunicaciones*, or “COFETEL”) cease to regulate Telmex’s pricing, the resulting competitive climate could have a material adverse effect on our business, financial condition and results of operations.

**The Federal Tax and Administrative Court may rescind or nullify COFETEL’s resolution approving a reduction in tariffs for termination of national long distance calls from Axtel to Telmex, which could have a material adverse effect on our business and results of operations.**

In March 2009, COFETEL resolved an interconnection dispute between the Company and Telmex with respect to the fees applicable for termination of national long distance calls from the Company to Telmex with respect to 2009. In this decision COFETEL approved a reduction in the interconnection fees charged by Telmex for terminating national long distance calls in their network with respect to those cities where Telmex does not have interconnection access points. These fees were reduced from Ps. 0.75 (US\$0.0574 calculated with the December 31, 2009 exchange rate of Ps. 13.0587 per U.S. dollar) per minute to US\$0.0105 or US\$0.0080 per minute (depending on the place where the interconnection is made).

Nevertheless, Telmex continues to invoice the Company for the termination of long distance calls at rates which applied prior to COFETEL’s decision. As of December 31, 2009, the difference between the amounts paid by us according to the new rates and the amounts invoiced by Telmex is approximately Ps. 64.9 million before Value Added Tax, for which the Company has not established any reserves.

Telmex filed a complaint before the Federal Tax and Administrative Court (*Tribunal Fiscal y de Justicia Administrativa*) requesting the annulment of the COFETEL decision. See “Business—Regulatory Proceedings.” Currently, this proceeding is in the discovery stage and resolution is pending.

Effective January 26, 2010, the Federal Tax and Administrative Court granted an injunction requested by Telmex which suspended the effectiveness of the interconnection rates established by COFETEL. However, this injunction ceased to be effective on February 11, 2010, after the Company posted a surety bond granting an indemnity to Telmex, in the event that Telmex obtains a favorable judgment (i.e. the annulment of the new interconnection fees under COFETEL’s decision). Such surety bond only covers lost interest on any unpaid amounts by the Company to Telmex.

We believe that the Federal Tax and Administrative Court will rule in our favor by confirming the decision issued by COFETEL; we have therefore recognized costs based on the fees approved by COFETEL. However, we cannot assure that the Federal Court will rule in our favor, in which case, COFETEL’s decision may be declared null and void, having as a possible result an increase to the rates that the Company will have to pay Telmex with respect to the year 2009, and also, a possible retroactive application of the pre-existing Ps. 0.75 tariff, thereby compelling us to pay any unpaid amounts invoiced by Telmex during 2009. An adverse ruling from the Federal Tax and Administrative Court could have a material adverse effect on our business and results of operations.

With respect to the interconnection fees arising from the termination of national long distance calls payable by the Company to Telmex in 2010, an interconnection dispute between the Company and Telmex is still pending before the COFETEL. We believe that, consistent with its decision with respect to 2009, COFETEL will decide in our favor by authorizing the continued application of the reduced interconnection fee, in which case, this decision may also be challenged by Telmex.

The Avantel interconnection agreement with Telmex provides for a non-discriminatory and most favorable customer treatment to Avantel, pursuant to which, along with non-discriminatory principles set forth under applicable law, Avantel applied the same fees determined payable by Axtel to the services provided to Avantel by Telmex.



Nevertheless, Telmex continues to invoice Avantel for the termination of long distance calls at rates which were effective prior to COFETEL's decision mentioned above. As of December 31, 2009, the difference between the amounts paid by Avantel according to the new rates and the amounts invoiced by Telmex is approximately Ps. 699.5 million before Value Added Tax, for which there is no reserve.

In February 2010, COFETEL resolved an interconnection dispute between Avantel and Telmex with respect to the applicable fees for the termination of long distance calls from Avantel to Telmex with respect to the year ended December 31, 2009. Pursuant to this decision, COFETEL approved a reduction in the rates for termination of long distance calls applicable to those cities where Telmex does not have interconnection access points. These rates were reduced from Ps. 0.75 (US\$0.0574 calculated with the December 31, 2009 exchange rate of Ps. 13.0587 per U.S. dollar) per minute to US\$0.0126, US\$0.0105 or US\$0.0080 per minute, depending on the place where the interconnection is made.

Based on reduced rates approved in this decision, Avantel paid Telmex approximately Ps. 20.0 million in excess of what Avantel should have paid if the reduced rates authorized by COFETEL would had been applied effective during 2009. Management believes that Telmex will probably challenge this decision. We and our legal advisors are evaluating the steps to be followed. An adverse ruling from the Federal Tax and Administrative Court could have a material adverse effect on our business and results of operations.

**We rely on Telmex to maintain our leased last-mile links.**

We maintain a number of dedicated links and last-mile-access infrastructure under lease agreements with Telmex. If Telmex breaches the agreed contractual conditions, or an agreement is not renewed upon its expiration, and Telmex discontinues the provision of services before we are able to link these customers to our own network, there could be a material adverse effect on our operations and an adverse effect on our business, financial condition and results of operations.

**One of our technology suppliers has filed for creditor protection under Canada's Companies' Creditors Arrangement Act ("CCAA") and under the United States Bankruptcy Code.**

We maintain and buy network infrastructure from Nortel Networks that requires maintenance and new spare parts from time to time. Currently, this vendor has filed for creditor protection under Canada's CCAA, a similar provision to filing under Chapter 11 of the United States Bankruptcy Code. On December 23, 2009, Nortel and GENBAND, Inc. announced their intent to enter into a asset sale agreement providing for the sale of substantially all of the global assets of Nortel's Carrier VoIP and Application Solutions business to GENBAND, which is subject to court approval. If the sale is approved, GENBAND will take over the maintenance of the network infrastructure we acquired from Nortel, as well as the supply of replacement and spare parts. However, in the event the sale is not approved, and the financial condition of this vendor deteriorates, we could be adversely affected due to the lack of maintenance and spare parts for the equipment already deployed, jeopardizing the future of this infrastructure. Equipment which becomes damaged or obsolete due to lack of upgrades would have to be replaced with other equipment in order for us to continue providing services in an uninterrupted manner.

**A system failure could cause delays or interruptions of service, which could cause us to lose customers.**

To be successful, we will need to continue to provide our customers reliable service over our network. Some of the risks to our network and infrastructure include:

- physical damage to access lines;
- power surges or outages;
- software defects; and
- disruptions beyond our control.

Disruptions may cause interruptions in service or reduced capacity for customers, either of which could cause us to lose customers and incur additional expenses.

**Under Mexican law, our concessions could be expropriated or temporarily seized.**

Pursuant to the Mexican Federal Telecommunications Law (*Ley Federal de Telecomunicaciones*) enacted in 1995, as amended, the public telecommunications networks are considered public domain. Under such law, holders of concessions to install operate and develop public telecommunications networks are subject to the provisions of the Mexican Federal Telecommunications Law and any other provision contained in the concession title. The Mexican Federal Telecommunications Law provides, among other things, for the following:

- rights and obligations granted under the concessions to install, operate and develop public telecommunications networks may only be assigned with the prior authorization of the SCT;
- neither the concession nor the rights thereunder or the related assets may be assigned, pledged, mortgaged or sold to any government or country; and
- the Mexican government (through the SCT) may expropriate or temporarily seize the assets related to the concessions in the event of natural disasters, war, significant public disturbance or threats to internal peace or for other reasons relating to economic or public order.

Mexican law sets forth the process for indemnification for direct damages arising out of the expropriation or temporary seizure of the assets related to the concessions, except in the event of war. However, in the event of expropriation, we cannot assure you that the indemnification will equal the market value of the concessions and related assets or that we will receive such indemnification in a timely manner. Mexican law does not prohibit a grant of a security interest by the concessionaire to its creditors (except for security granted to a foreign government or country) in the concessions and the assets, *provided* that all procedural laws are complied with; however, if such security interest is enforced, the assignee must comply with the Mexican Federal Telecommunications Law's provisions related to concessionaires, including, among others, the requirement to receive the authorization by the SCT to be a holder of the concession.

**We could lose or encounter unfavorable conditions and fees with respect to our concessions.**

Under our concessions, we are subject to various financial and technical conditions imposed by the SCT. We cannot assure you that we will continue to meet these conditions. Failure to meet or to obtain a waiver or modification of these conditions can result in a fine, loss of surety or termination of the concession. Furthermore, our concessions are of a fixed duration and are scheduled to expire between 2018 and 2026. We cannot assure you of our ability to renew our concessions nor of the terms of any such renewal. The renewal fee is determined at the time of renewal. A failure to renew or maintain our concessions could have a materially adverse effect on our business.

**The regulatory authorities could require us to offer services in certain geographical areas where we may experience a lower operating margin.**

The SCT has granted us the necessary permits to provide services in the whole Mexican territory. Some of our concessions require us to offer services in certain geographical areas where we do not currently provide services. With respect to those geographical areas in which we were required to provide such services by December 2008, we have complied with such coverage requirements. If needed in the future, we may request extensions from the SCT in order to comply with the terms of some of our concessions. We may also be required to provide services in geographical areas where we may experience a low operating margin with respect to such services. If we do not obtain the necessary extensions when required, or if we are required to provide services in areas where we do not currently provide services or in geographical areas where we may experience a low operating margin with respect to such services, our results of operations and financial condition may be adversely affected.



**We depend on revenues from certain highly competitive markets.**

High-volume business customers are among the most attractive niches in the telecommunications market. This niche is being pursued by a number of carriers that offer competitive telecommunications services solutions in order to gain these accounts. The residential customer market is also being targeted by a number of carriers, including Televisa and Nextel through their recent alliance, which may further increase competition in that market. Losing some of these customers could lead to a significant loss of revenue and lower operating income.

**We depend on revenues from long distance services.**

Prices for long distance services have been declining as new products such as voice over internet protocol, or VoIP, continue to gain acceptance. If we are unable to replace revenues lost from long distance with revenues from other services, such as local, data or integrated services, it could have a material adverse effect on our business, financial condition and results of operations.

**We may need additional financing.**

We may require additional financing in the future to fund our operations. We operate a capital intensive business. Since our inception and as of December 31, 2009, we have invested over Ps. 29,074.3 million in building our infrastructure. We expect to make additional investments in future years as we selectively expand our network into other areas of Mexico in order to exploit market opportunities as well as to maintain our existing network and facilities. In addition, we operate in a highly regulated industry and we face the regulatory risk of having a Mexican governmental agency mandate increased capital expenditures or our incurrence of other expenses not currently contemplated. We cannot assure you that we will have sufficient resources to make such investments or cover potential expenses mandated by governmental agencies and that, if needed, any financing will be available in the future or on terms acceptable to us. In addition, our ability to incur additional indebtedness will be restricted by the terms of agreements currently in place or into which we may enter in the future.

Adverse conditions in the Mexican and international credit markets, including higher interest rates, reduced liquidity or decreased interest by financial institutions in lending to us, have in the past and may in the future increase our cost of borrowing or refinancing maturing indebtedness, with adverse consequences to our financial condition and results of operations. We cannot assure you that we will be able to refinance any indebtedness we may incur or otherwise obtain funds by selling assets or raising equity to make required payments on maturing indebtedness.

**The technology we use may be made obsolete by the technology used by our competitors.**

Our fixed wireless system, as well as our fiber optic network, point-to-multipoint and point-to-point infrastructure, may not be as efficient as technologies used in the future by our competition. We have relied heavily on the continued performance of wireless technology. Technological changes or advances in alternative technologies may adversely affect our competitive position and require us to reduce our prices, substantially increase capital expenditures and/or write down obsolete technology.

**If our current churn rate increases our business could be negatively impacted.**

The cost of acquiring a new customer is much higher than the cost of maintaining an existing customer. Accordingly, customer deactivations, or churn, could have a material negative impact on our operating income, even if we are able to obtain one new customer for each lost customer. Our average monthly churn rate has been stable during the 24 month period ended December 31, 2009 at approximately 1.8%, which is higher than that of our main competitor. Our churn rate mainly results from customer deactivations due to non-payment of bills. If we experience an increase in our churn rate, our ability to achieve revenue growth could be materially impaired. In addition, a decline in general economic conditions could lead to an increase in churn, particularly among our residential customers.

**Restrictive covenants in our credit facility and the indentures may restrict our ability to pursue our business strategies.**

Our 2012 Term Loan Facility, the indenture governing our 7<sup>5</sup>/<sub>8</sub>% senior notes due 2017 (the “2017 Notes”) and the indenture governing the existing notes and the new notes, limit, and upon entry, our New Revolving Credit Facility will limit, our ability, among other things, to:

- incur additional indebtedness or contingent obligations;
- pay dividends or make distributions to our stockholders;
- repurchase or redeem our stock;
- make investments;
- grant liens;
- make capital expenditures;
- enter into transactions with our stockholders and affiliates;
- sell assets; and
- acquire the assets of, or merge or consolidate with, other companies.

In addition, our 2012 Term Loan Facility requires us and upon entry, our New Revolving Credit Facility will require us, to maintain financial ratios. These financial ratios include a minimum net worth, a maximum total leverage ratio and minimum fixed charge coverage ratio. We may not be able to maintain these ratios in the future. Covenants in our credit facility and the 2017 Notes indentures and the indenture governing the new notes may also impair our ability to finance future operations or capital needs or to enter into acquisitions or joint ventures or engage in other favorable business activities.

If we default under our credit facility, or the indenture governing the 2017 Notes or indenture governing the existing notes, the lenders under our credit facility and the noteholders under the 2017 Notes and the existing notes indenture, as applicable, could require immediate repayment of the entire principal amount of such debt. If those lenders or noteholders, as applicable, require immediate repayment, we will not be able to repay them and also repay the new notes in full.

**The benefits from the acquisition of Avantel could be eroded in the future or cause the combined business to fail to meet our expectations.**

Our integration of the Axtel and Avantel businesses started in December 2006 and most of the material aspects of that process were completed in 2008. However, it is still possible that business practices from each of the former two companies might not be fully integrated at all times which could harm our revenues and profitability and cause us to grow more slowly than we currently anticipate. Our relative lack of experience in making several acquisitions in the past could increase these risks for us.

**Risks Relating to the Mexican Telecommunications Industry**

**We operate in a highly regulated industry.**

As a provider of public services, we are subject to extensive regulation. Although the basic regulatory framework governing telecommunications has been in existence since 1995, it may undergo changes from time to time, including changes that may materially and adversely affect our business, operations, financial condition and prospects.

On July 5, 2008, fixed and mobile phone number portability was implemented in Mexico. As of this date, the portability service has been operating properly, with the exception of certain third party networks that still take longer than the timeframe established by COFETEL to route calls to the receiving user. We cannot predict the consequences that portability will have on the market or how it might affect our business.

In 2008, the Mexican Antitrust Commission (*Comisión Federal de Competencia*, or “CFC”) issued a preliminary declaration, stating that all fixed and mobile service providers may have significant market power in the traffic termination market. We are unable to predict if the final declaration will take this position, which could adversely affect our business and subject us to additional legal liability or obligations. If we are declared to have significant power in the traffic termination market in a final declaration by the CFC, our rates could be regulated and we could be required to comply with certain levels of services and information quality.

The operation of telecommunications systems in Mexico, including ours, has been subject to laws and regulations administered by the SCT and COFETEL. An amendment to the internal operating rules of the SCT was issued during 2008. These new rules will cause an amendment to the internal operating rules of COFETEL in the near future. The resulting regulatory changes could adversely affect our business and subject us to additional legal liability or obligations, as the decisions to be taken by the SCT and COFETEL could be delayed or take longer periods of time to be resolved.

**Recently announced auction processes for wireless spectrum and capacity on CFE’s fiber optic network may result in the formation of new competitors or stronger competitive positions of existing telecommunications companies.**

In early 2010, the SCT and COFETEL released the rules for the auctions of 120 MHz at 1.7/2.1 GHz and 90 MHz at 1.9 MHz spectrums, and capacity available in one pair of dark fiber on CFE’s 19,500 km. fiber optic network. The wireless spectrums, particularly the 1.7/2.1 GHz frequency, could promote the entry of new competitors or strengthen existing competitors’ ability to provide mobile services that may substitute services currently provided by us. The dark fiber capacity auction could also attract new entrants into the wholesale capacity business, potentially reducing revenues from services currently provided by us. If we are unable to generate sufficient traffic and increased revenues to offset the impact of these events, our operating margins may be negatively affected we may be required to increase capital expenditures and write off obsolete technology.

**If the Mexican government grants more concessions or amends existing concessions, the value of our concessions could be severely impaired.**

The Mexican government regulates the telecommunications industry. Our concessions are not exclusive and the Mexican government has granted and has discretion to grant additional concessions covering the same geographic regions. We cannot assure you that additional concessions to provide services similar to those we provide will not be granted and that the value of our concessions and competition levels will not be adversely affected as a result.

**Decreases in market rates for telecommunication services could have a material adverse effect on our business, results of operation and our financial condition.**

We expect the Mexican telecommunications market to continue to experience rate pressure, primarily as a result of:

- increased competition and focus by our competitors on increasing market share; and
- recent technological advances that permit substantial increases in the transmission capacity of both new and existing fiber optic networks resulting in long distance overcapacity.

Continued rate pressure could have a material adverse effect on our business, financial condition and operating results if we are unable to generate sufficient traffic and increased revenues to offset the impact of the decreased rates on our operating margin.

**Fraud could increase our expenses.**

The fraudulent use of telecommunications networks could impose a significant cost upon service providers, who must bear the cost of services provided to fraudulent users. We may suffer a loss of revenue as a result of fraudulent use and incur an additional cash cost due to our obligation to reimburse carriers for the cost of services provided to fraudulent users. Although technology has been developed to combat this fraudulent use and we have installed it in our network, this technology does not eliminate the impact of fraudulent use entirely. In addition, because we rely on other long distance carriers to terminate our calls on their networks, some of which do not have anti-fraud technology in their networks, we may be particularly exposed to this risk in our long distance service.

**Risks Relating to Mexico****Our business and customers may be negatively affected by the current global and Mexican financial downturn.**

The economic and market conditions of Mexico, as well as the financial condition and operating results of our company, are greatly affected by worldwide economic conditions. The recent global deterioration of economic conditions has led to reductions in available capital and liquidity, reductions in equity and currency values, extreme volatility in credit, equity and fixed income markets and general economic uncertainty in Mexico and around the world. Continuing deterioration may harm our financial condition, inhibit demand for our services and adversely affect our suppliers and customers. The effects of the current economic situation are extremely difficult to forecast and mitigate.

**Health epidemics and other outbreaks in Mexico may affect our business operations.**

Our business could be adversely affected by the effects of avian flu, severe acute respiratory syndrome, SARS, H1N1 flu or another epidemic or outbreak. In April 2009, an outbreak of H1N1 flu occurred in Mexico and the United States and has spread to more than 70 countries, leading the World Health Organization to declare the first global flu pandemic in over 40 years. Any prolonged occurrence or recurrence of avian flu, SARS, H1N1 flu or other adverse public health developments in Mexico may have a material adverse effect on our business operations. Our operations may be impacted by a number of health-related factors, including, among other things, quarantines or closures of our facilities and developments which could disrupt our operations, and a general slowdown in the Mexican economy. Any of the foregoing events or other unforeseen consequences of public health problems could adversely affect our business and results of operations. We have not adopted any written preventive measures or contingency plans to combat any future outbreak of avian flu, SARS, H1N1 flu or any other epidemic.

**Weakness in the Mexican economy could adversely affect our business, financial condition and results of operations.**

Our operations, results and financial condition are dependent in part upon the level of economic activity in Mexico. Mexico experienced a period of slow economic growth from 2001 through 2003, primarily as a result of the downturn in the U.S. economy. According to Banco de Mexico estimates, in 2001, Mexico's gross domestic product ("GDP") declined by 0.2%, while inflation reached 4.4%. In 2002, GDP grew by 0.8% and inflation reached 5.7%. In 2003, GDP grew by 1.4% and inflation reached 4.0%. In 2004, GDP grew by 4.0% and inflation increased to 5.2%. In 2005, GDP grew by 3.2% and inflation reached 3.3%. In 2006, GDP increased by 4.8% and inflation increased to 4.1%. In 2007, GDP increased by 3.6% and inflation reached 3.8%. In 2008, GDP increased by 1.3% and inflation increased to 6.5%.

Mexico also has, and is expected to continue to have, high real and nominal interest rates. The interest rates on 28-day Mexican government treasury securities (certificados de la tesorería) averaged approximately 6.8%, 9.2%, 7.2%, 7.2%, 7.7% and 5.4% for 2004, 2005, 2006, 2007, 2008 and 2009, respectively. Relative to the

U.S. Dollar, the peso appreciated by 0.8% in 2004, appreciated by 4.7% in 2005, depreciated by 1.6% in 2006, depreciated by 1.1% in 2007, depreciated by 26.70% in 2008 and appreciated by 5.6% in 2009, all in nominal terms. Accordingly, to the extent that we incur peso-denominated debt in the future, it could be at high interest rates.

As a consequence of the global recession and economic slowdown during 2008 and 2009, the Mexican economy entered into a recession. The GDP growth in 2009 contracted 6.5% and the twelve-month accumulated inflation increased 3.6%. As a consequence, the Mexican consumer confidence index decreased to an eight-year low of 80.1 points, with a corresponding impact on consumption. As a result, consumer purchasing power may decrease and demand for telecommunications services may also decrease. The current recession could affect our operations to the extent that we are unable to reduce our costs and expenses in response to falling demand. These factors could result in a decrease in our revenues and profit.

#### **Political events in Mexico may affect our operations.**

Mexican President Felipe Calderón Hinojosa, of the political party Partido Acción Nacional (“PAN”), may implement significant changes in laws, public policies and/or regulations that could affect Mexico’s political and economic situation, which could adversely affect our business. Any change in the current telecommunications regulatory policies could have a significant effect on Mexican telecommunications service providers, including us, variations in interest rates, demand for our services, market conditions, and the prices of and returns on Mexican securities.

Furthermore, following Mr. Calderón’s election in 2006, the Mexican Congress became politically divided, as the PAN does not have majority control. Elections for the Mexican Senate and House of Representatives and for the governorship of certain states of the Republic took place on July 5, 2009, giving the Partido Revolucionario Institucional (“PRI”) a majority in the legislature. The lack of alignment between the legislature and the President could result in deadlock and prevent the timely implementation of political and economic reforms, which in turn could have a material adverse effect on Mexican economic policy and on our business. It is also possible that political uncertainty may adversely affect Mexico’s economic situation.

Social and political instability in Mexico or other adverse social or political developments in or affecting Mexico could adversely affect our business, financial condition and result of operations, as well as market conditions and prices for our securities. These and other future developments in the Mexican political or social environment may cause disruptions to our business operations and decreases in our sales and net income.

#### **Developments in other countries could adversely affect the Mexican economy, the market value of our securities and our results of operations.**

As is the case with respect to securities of issuers from emerging markets, the market value of securities of Mexican companies is, to varying degrees, affected by economic and market conditions in other emerging market countries. Although economic conditions in these countries may differ significantly from economic conditions in Mexico, investors’ reactions to developments in any of these other countries may have an adverse effect on the market value of securities of Mexican issuers. In recent years, for example, prices of both Mexican debt securities and Mexican equity securities dropped substantially as a result of developments in Russia, Asia and Brazil.

In addition, the correlation between economic conditions in Mexico and the U.S. has sharpened in recent years as a result of NAFTA and increased economic activity between the two countries. As a result of the slowing economy in the United States and the uncertain impact it could have on general economic conditions in Mexico and the United States, our financial condition and results of operations could be adversely affected. In addition, due to recent developments in the international credit markets, capital availability and cost could be significantly affected and could restrict our ability to obtain financing or refinance our existing indebtedness on favorable terms, if at all.

**High interest rates in Mexico could increase our financing and operating costs.**

Mexico historically has had high real and nominal interest rates. According to Banco de Mexico, the interest rates on 28-day Mexican government treasury securities, CETES, averaged 21.3%, 15.3% and 11.3% for 1999, 2000 and 2001, respectively. Although average rates for 2003, 2004, 2005, 2006, 2007, 2008 and 2009 were 6.2%, 6.8%, 9.2%, 7.2%, 7.2%, 7.7% and 5.4%, respectively, we cannot assure you that interest rates will remain at their current rates. Thus, if we are forced to incur Mexican Peso-denominated debt in the future, it may be at interest rates higher than the current rates.

**Devaluation of Mexican currency could adversely affect our financial condition.**

While our revenues are almost entirely denominated in pesos, the substantial majority of our capital expenditures and approximately 85% of our contracted debt as of December 31, 2009 is denominated in U.S. dollars (however, including derivative instruments this percentage is reduced to approximately 82%). The value of the Mexican Peso has been subject to significant fluctuations with respect to the U.S. dollar in the past and may be subject to significant fluctuations in the future. During the year ended December 2004 and 2005, the peso appreciated 0.8% and 4.7%, respectively (in nominal terms) relative to the U.S. dollar. In 2006 and 2007 the peso depreciated 1.6% and 1.1% (in nominal terms) respectively, relative to the U.S. dollar. In 2008, as a consequence of the global economic and financial crisis, the peso depreciated 26.7% against the U.S. dollar in nominal terms. In 2009, the peso has appreciated 5.6% against the U.S. dollar in nominal terms. Further declines in the value of the peso may also result in disruption of the international foreign exchange markets. This may limit our ability to transfer or convert pesos into U.S. dollars and other currencies and adversely affect our ability to meet our current U.S. dollar-denominated obligations and any other U.S. dollar-denominated obligations that we may incur in the future. While the Mexican federal government does not currently restrict the ability of Mexican or foreign persons or entities to convert pesos into U.S. dollars or other currencies, the Mexican federal government could institute restrictive exchange control policies in the future.

**Our financial statements do not give you the same information as financial statements prepared under U.S. GAAP.**

We prepare our financial statements in accordance with Mexican FRS. These principles differ in significant respects from U.S. GAAP, including, but not limited to, the treatment of the capitalization of pre-operating expenses, the amortization of frequency rights, the capitalization of interest and deferred income taxes and employees' profit sharing, and in the presentation of cash flow information. In particular, until December 31, 2007 all Mexican companies were required to incorporate the effects of inflation directly in their accounting records and in published financial statements. For these and other reasons, the presentation of Mexican financial statements and reported earnings may differ from that of companies in other countries. See "Management's Discussion and Analysis of Financial Condition and Results of Operations of Axtel—Summary of Differences between Mexican FRS and U.S. GAAP."

**Risks Relating to the New Notes**

**Our indebtedness could adversely affect our financial condition and impair our ability to fulfill our obligations under the notes.**

Our ability to meet our debt service requirements will depend on our future performance, which is subject to a number of factors, many of which are outside our control. We cannot assure you that we will generate sufficient cash flow from operating activities to meet our debt service and working capital requirements.

As of December 31, 2009 and December 31, 2008, we had approximately Ps. 10,107.7 and Ps. 9,791.1 million of debt and accrued interest, respectively, and our ratio of net debt to Adjusted EBITDA for the years ended December 31, 2009 and December 31, 2008 was 2.3x and 2.1x, respectively.



Our level of indebtedness may have important negative effects on our future operations, including:

- impairing our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions or other general corporate purposes;
- requiring us to dedicate a substantial portion of our cash flow to the payment of principal and interest on our indebtedness, which reduces the availability of our cash flow to fund working capital, capital expenditures, acquisitions and other general corporate purposes;
- subjecting us to the risk of increased sensitivity to interest rate increases on our indebtedness with variable interest rates, including our borrowings under our credit facilities;
- increasing the possibility of an event of default under the financial and operating covenants contained in the agreements governing our and our subsidiary guarantors' outstanding indebtedness; and
- limiting our ability to adjust to rapidly changing market conditions, reducing our ability to withstand competitive pressures and making us more vulnerable to a downturn in general economic conditions or our business than our competitors with less debt.

If we are unable to generate sufficient cash flow from operations in the future to service our debt, we may be required to refinance all or a portion of our existing debt, or to obtain additional financing. We cannot assure you that any such refinancing would be possible or that any additional financing could be obtained. Our inability to obtain such refinancing or financing may have a material adverse effect on us.

**We and our subsidiary guarantors may incur substantially more debt, which could further exacerbate the risks associated with our indebtedness.**

We may be able to incur substantial additional debt in the future. Although the agreements governing our and our subsidiary guarantors' outstanding indebtedness contain restrictions on the incurrence of additional indebtedness, these restrictions are subject to a number of qualifications and exceptions, and the indebtedness incurred in compliance with these restrictions could be substantial. Also, these restrictions do not prevent us or our subsidiary guarantors from incurring obligations that do not constitute "indebtedness" as defined in the relevant documents. Adding new debt to our current indebtedness levels would increase our leverage. The related risks that we now face could intensify.

**The instruments governing our indebtedness, including the new notes offered hereby, contain cross-default provisions that may cause all of the debt issued under such instruments to become immediately due and payable as a result of a default under an unrelated debt instrument.**

The indenture governing the notes contains numerous restrictive covenants. Instruments governing our other indebtedness also contain certain affirmative and negative covenants and require us and our subsidiaries to meet certain financial ratios and tests. Our failure to comply with the obligations contained in the indenture or other instruments governing our indebtedness could result in an event of default under the applicable instrument, which could then result in the related debt and the debt issued under other instruments becoming immediately due and payable. In such event, we would need to raise funds from alternative sources, which may not be available to us on favorable terms, on a timely basis or at all. Alternatively, such default could require us to sell our assets and otherwise curtail operations in order to pay our creditors.

**The new notes and the guarantees, together with the existing notes, will be unsecured and effectively subordinated to our secured indebtedness.**

The notes and the obligations of the subsidiary guarantors under their respective guarantees will not be secured by any of our assets. We are a party to certain financing facilities, which are secured by specific collateral, which cover the outstanding amount in each of the facilities. See "Description of Other Indebtedness." As of December 31, 2009, we had US\$12.0 million of secured debt outstanding. These credit facilities have specific guarantees, which cover only the amount that is outstanding.



If we become insolvent or are liquidated, or if payment under any secured debt is accelerated, the lenders thereunder would be entitled to exercise the remedies available to a secured lender. Accordingly, the lenders would have priority over any claim for payment under the notes to the extent of the value of the assets that constitute its collateral. If this were to occur, it is possible that there would be no assets remaining from which claims of the holders of the notes could be satisfied. Further, if any assets did remain after payment of these lenders, the remaining assets might be insufficient to satisfy the claims of the holders of the notes and holders of other unsecured debt that is deemed the same class as the notes, and potentially all other general creditors who would participate ratably with holders of the notes.

**Restrictive covenants in our debt agreements may restrict the manner in which we can operate our business.**

The agreements governing our and our subsidiary guarantors' outstanding indebtedness, including the indenture governing the existing notes and the supplemental indenture governing the notes offered hereby, limit, and upon entry, our New Revolving Credit Facility will limit, among other things, our ability and the ability of our restricted subsidiaries to:

- borrow money or issue guarantees;
- pay dividends, redeem capital stock or make other restricted payments;
- create liens to secure indebtedness;
- make certain investments;
- sell certain assets;
- pledge assets;
- participate in joint-venture agreements;
- enter into transactions with our affiliates; and
- merge with another entity or sell substantially all of our assets.

If we fail to comply with these covenants, we would be in default under our credit facility and the indentures, and the principal and accrued interest on our outstanding indebtedness may become due and payable. See "Description of Other Indebtedness" and "Description of the Notes—Certain Covenants." In addition, our future indebtedness agreements may contain additional affirmative and negative covenants which could be more restrictive than those contained in the instruments governing our existing indebtedness.

The "restricted payments" covenant in the indenture governing the notes allows us to pay dividends, redeem capital stock and make other restricted payments in an amount at least up to 50% of the Adjusted Consolidated Net Income accrued during the period beginning on April 1, 2009, plus the aggregate net cash proceeds we have received from issuances of our capital stock since September 22, 2009. As of December 31, 2009, 50% of the Adjusted Consolidated Net Income accrued during the period of April 1, 2009 to December 31, 2009 totaled US\$20.1 million. Since September 22, 2009, we have not issued any capital stock, therefore, we have not received any cash proceeds from issuances of our capital stock. See "Description of the Notes—Certain Covenants—Limitation on Restricted Payments."

**We may not have the ability to repurchase the notes upon a change of control as required by the indenture.**

Upon the occurrence of a change of control (as defined in the indenture), we will be required to offer to purchase all outstanding notes at 101% of their principal amount plus accrued and unpaid interest to the date of repurchase. Upon such a change of control, we may not have sufficient funds available to repurchase all of the notes tendered pursuant to this requirement. In addition, we may be prohibited by future credit facilities from repurchasing any of the notes unless the lenders thereunder consent to such repurchase. Our failure to repurchase the notes would be a default under the indenture governing the notes, which would, in turn, be a default under our credit facility, the indenture governing the existing notes and the new notes and, potentially, other debt. If the payment of any debt were to be accelerated, we might be unable to repay these amounts or make the required repurchase of the notes. See "Description of the Notes—Optional Redemption."

**We may not be able to make payments in U.S. dollars.**

In the past, the Mexican economy has experienced balance of payments deficits and shortages in foreign exchange reserves. While the Mexican government does not currently restrict the ability of Mexican or foreign persons or entities to convert pesos to foreign currencies, including U.S. dollars, it has done so in the past and could do so again in the future. We cannot assure you that the Mexican government will not implement a restrictive exchange control policy in the future. Any such restrictive exchange control policy could prevent or restrict our access to U.S. dollars to meet our U.S. dollar obligations and could also have a material adverse effect on our business, financial condition and results of operations. We cannot predict the impact of any such measures on the Mexican economy.

**An active trading market may not develop for the new notes, which may limit your ability to resell them.**

There is currently no established trading market for the new notes. An application has been submitted to have the new notes traded on the Euro MTF, a market of the Luxembourg Stock Exchange. We do not intend to list the new notes on any other stock exchange or seek their admission for trading in the National Association of Securities Dealers Automated Quotation System and we may delist the notes from the Luxembourg Stock Exchange at any time, should they become listed on that exchange. Although the initial purchasers have advised us that they intend to make a market in the new notes, they are not obligated to do so, and they may cease to do so at any time without notice. The lack of an active trading market for the new notes would have a material adverse effect on the market price and liquidity of the new notes. If a market for the new notes develops, the new notes may trade at a discount from their initial offering price.

In addition, you may not be able to sell your new notes at a particular time or at a price favorable to you. Future trading prices of the new notes will depend on many factors, including:

- our operating performance and financial condition;
- the interest of securities dealers in making a market;
- the market for similar securities;
- prevailing interest rates;
- changes in earnings estimates or recommendations by research analysts who track our notes or the notes of other companies in our industry;
- changes in general economic conditions;
- acquisitions, strategic alliances or joint ventures involving us or our competitors; and
- other developments affecting us, our industry or our competitors.

Historically, the market for non-investment grade debt has been subject to disruptions that have caused substantial volatility in prices. The market for the new notes, if any, may be subject to similar disruptions. A disruption may have a negative effect on you as a holder of the new notes, regardless of our prospects or performance.

**The new notes are subject to restrictions on transfer within the United States or to U.S. persons and may be subject to transfer restrictions under the laws of other jurisdictions.**

We have not and do not intend to register the new notes under the U.S. Securities Act or any U.S. state securities laws, and we have not undertaken to conduct any registered exchange offer for the new notes. Accordingly, you may not offer the new notes for sale in the United States or to U.S. persons (as defined in Regulation S), except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the U.S. Securities Act and applicable state securities laws, or pursuant to an effective

registration statement. Furthermore, we have not registered the new notes under any other country's securities laws. It is your obligation to ensure that your offers and sales of the new notes within the United States and elsewhere comply with applicable securities laws. See "Notice to Investors."

**The indenture governing the notes contains periodic reporting requirements that are different and less burdensome than would be applicable to us if we had agreed to register the notes following the closing of the offering.**

Effective January 5, 2010, we no longer file periodic reports with the SEC. Moreover, the indenture governing the notes does not require us to file such reports or other information. The indenture requires us to provide annual and quarterly reports, including English language translations of all our reports filed with the *Bolsa Mexicana de Valores* (the "Mexican Stock Exchange"), to the holders of notes and the trustee. The requirements of the indenture, however, are more limited in certain respects than those applicable to public companies under the Exchange Act. See "Description of the Notes—Certain Covenants—Reports to Holders."

**You may not be able to effect service of process on us, our subsidiaries or directors or to enforce in Mexican courts judgments obtained against us in the United States.**

We and our subsidiaries (except for Telecom Networks Inc.) are either public variable capital corporations, variable capital corporations, limited liability companies or fixed capital corporations organized under the laws of Mexico, and are headquartered, managed and operated outside of the United States (principally in Mexico). Most of our directors and officers reside in Mexico. All or a substantial portion of our assets and the assets of most of our directors and officers are located outside of the United States (principally in Mexico). As a result, it may not be possible for the investors or holders of the notes to effect service of process outside of Mexico or within the United States upon us or such persons, or to enforce a judgment obtained in the United States against us or them outside of Mexico or in the United States courts that is based on the civil liability provisions under laws of jurisdictions other than Mexico including the federal and state securities laws or other laws of the United States.

We have been advised by our special Mexican counsel, D&A Morales y Asociados, S.C., that no treaty is in effect between the United States and Mexico calling for the mutual recognition and enforcement of their respective judgments. The recognition by Mexican courts of a judgment rendered in the United States is usually done under the principle of reciprocity, which means that Mexican courts would reexamine judgments rendered in the United States if such foreign country would reexamine Mexican judgments. Mexican courts may enforce judgments rendered in the United States through a homologation procedure consisting of the review by such Mexican courts of the foreign judgment to ascertain whether certain requirements of due process, reciprocity and public policy have been complied with, without reviewing the merits of the subject matter of the case; *provided* that all federal and state procedural requirements under Mexican law (as the applicable case may be), including laws concerning statute of limitations and expirations, are satisfied; and further *provided* that, among others:

- (1) such judgment is final in the rendering state and obtained in compliance with legal requirements of the jurisdiction of the court rendering such judgment and such judgment is in compliance with the terms set forth in the notes and all legal requirements as the case may be;
- (2) such judgment is strictly for the payment of a certain sum of money, based on an in personam action (*acción personal*) as opposed to an in rem action (*acción real*);

- (3) the judge or court rendering the judgment is considered to have jurisdiction and is competent to hear and judge on the subject matter of the case in accordance with accepted principals of international law that are compatible and analogous with Mexican laws, and the subject matter of the case was not of the exclusive jurisdiction of Mexican courts;
- (4) service of process in the action has been served personally on the defendant or on a duly appointed process agent;
- (5) such judgment does not contravene Mexican law, public policy of Mexico, international treaties or agreements binding upon Mexico or generally accepted principles of international law;
- (6) the applicable procedure under the laws of México with respect to the enforcement of foreign judgments (including issuance of a rogatory letter (*carta rogatoria*) by the competent authority of such jurisdiction requesting enforcement of such judgment and the certification of such judgment as authentic by the corresponding authorities of such jurisdiction in accordance with the laws thereof) is complied with;
- (7) the courts of such jurisdiction would enforce Mexican judgments as a matter of reciprocity;
- (8) the action in respect of which such judgment is rendered is not the subject matter of a lawsuit or legal proceedings among the same parties that is or are pending before a Mexican court, or was resolved by or conflicts with a definitive judgment previously rendered by a Mexican court that has previously served process or delivered a rogatory letter (*carta rogatoria*) to the competent authorities in accordance with the Mexican law;
- (9) the court that rendered such judgment has jurisdiction over the debtor as recognized by the courts of Mexico and in accordance with its conflict of laws rules; and
- (10) the judgment fulfills all necessary requirements to be considered authentic.

Furthermore, there is doubt as to the enforceability, in actions originated in Mexico, of liabilities based in whole or in part on the United States federal or state securities laws and as to the enforceability of judgments obtained in the United States in actions based in whole or in part on the civil liability provisions of United States federal or state securities laws.

**Payment of judgments entered against us in Mexico will be in pesos, which may expose you to exchange rate risks.**

If proceedings to enforce our obligations under the notes are brought in Mexico, Mexican law permits us to pay a resulting judgment in pesos. Under the *Ley Monetaria de los Estados Unidos Mexicanos* (the “Mexican Monetary Law”), an obligation payable in Mexico in a currency other than pesos may be satisfied in pesos at the exchange rate in effect on the date the payment is made. This rate is currently determined and published by Banco de Mexico every business day.

Under Mexico’s *Ley de Concursos Mercantiles* (the “Mexican Bankruptcy Law”), upon our declaration of insolvency (*Concurso Mercantil*) or bankruptcy, or in the event that actions and claims are initiated in the courts of Mexico, our obligations under the notes:

- (i) would be converted into pesos at the exchange rate published by Banco de Mexico prevailing at the time of such declaration and would subsequently be converted into *Unidades de Inversion*, which is a unit pegged to the consumer price index determined by Banco de Mexico, and payment would occur at the time claims of our other creditors are satisfied;
- (ii) would be subject to any provisional remedy (“*providencia precautoria*”) which may be issued in such proceedings;
- (iii) would be dependent upon the outcome of the insolvency or bankruptcy proceedings;

- (iv) would not be adjusted to take into account depreciation of the peso against the dollar occurring after such declaration of insolvency or bankruptcy; and
- (v) would be subject to certain statutory preferences including tax, social security and labor claims and secured creditors.

Under the Mexican Bankruptcy Law, it is possible that in the event we are declared insolvent or bankrupt, any amount by which the stated principal amount of the notes exceeds their accreted value may be regarded as not mature and, therefore, claims of holders of the notes may be allowed only to the extent of the accreted value of the notes. Any provision that aggravates or makes more onerous the obligations of the insolvent entity by virtue of the filing of a petition of bankruptcy or insolvency (whether voluntary or involuntary) is considered invalid and may be deemed as if not included in the agreement under Mexican Law. It is believed that there are no Mexican precedents in insolvency or bankruptcy addressing this matter and there exists significant uncertainty as to how a Mexican court would measure the claims to holders of the notes.

**The collection of interest on interest may not be enforceable in Mexico.**

Mexican law does not permit the collection of interest on interest and, therefore, the accrual of default interest on past due ordinary interest accrued in respect of the notes may be unenforceable in Mexico.

**It is possible that the guarantees by our subsidiaries may not be enforceable.**

All of our current subsidiary guarantors are Mexican corporations or limited liability companies. The guarantees being given by the subsidiary guarantors provide a basis for a direct claim against the subsidiary guarantors. However, it is possible that such guarantees may not be enforceable. We have been advised by our special Mexican counsel, D&A Morales y Asociados, S.C., that the laws of Mexico may in some cases prevent their respective guarantees from being valid, binding and enforceable against such subsidiary guarantors in accordance with their terms. However, in the event that such a subsidiary guarantor is declared insolvent or bankrupt, the guarantee may be deemed to have been a fraudulent transfer and declared void if such subsidiary guarantor failed to receive fair consideration or reasonably equivalent value in exchange for such guarantee. In addition, under Mexican Bankruptcy Law, if we or any of the subsidiary guarantors are judicially declared insolvent or bankrupt, our obligations under the notes and each of such subsidiary guarantors' obligations under its guarantee will be subordinated to secured creditors and certain statutorily preferred creditors, such as those holding labor, tax and social security related claims, which will have preference over any other claims, including claims by any investor in respect of the notes or such guarantees. Furthermore, we have been advised that under Mexican laws, the validity of each guarantee is subject to the existence and validity of the obligation being guaranteed. As a consequence thereof, its enforcement is not independent or irrespective of such obligation being guaranteed. Furthermore, under Mexican law, a subsidiary guarantor may be released from its obligations under the guarantee if (i) the holder of the note gives us an extension for payment under the notes without the express consent of such subsidiary guarantor, or (ii) the company waives any cause that would otherwise release the company of its obligations under the notes, including expirations or statute of limitation provisions.

The obligation of each subsidiary guarantor may be subject to review under United States state or federal fraudulent transfer laws. Under such laws, if a court in a lawsuit by an unpaid creditor or representative of creditors of a subsidiary guarantor, such as a trustee in a bankruptcy of such subsidiary guarantor as debtor in possession, were to find that at the time such obligation was incurred such subsidiary guarantor, among other things, (a) did not receive fair consideration or reasonably equivalent value therefore and (b) (i) was insolvent, (ii) was rendered insolvent, (iii) was engaged in a business or transaction for which its remaining unencumbered assets constituted unreasonably small capital or (iv) intended to incur or believed that it would incur debts beyond its ability to pay such debts as they matured, such court could avoid such subsidiary guarantor's obligation and direct the return of any payments made thereunder to such subsidiary guarantor or to a fund for the benefit of its creditors. Moreover, regardless of the factors identified in the foregoing clauses (i) through (iv),

such court could avoid such obligation and direct such repayment if it found that the obligation was incurred with an intent to hinder, delay or defraud such subsidiary guarantor's creditors.

The measure of insolvency for purposes of the preceding paragraphs will vary depending upon the law of the jurisdiction being applied. Generally, however, an entity would be considered insolvent if it is unable to pay or satisfy its obligations as they become due, the sum of its debts is greater than all of its property (including collection rights) at a fair valuation or the present fair salable value of its assets is less than the amount that will be required to pay its probable liability on its existing debts as they become absolute and matured.

If the guarantees become unenforceable under the conditions described above, the notes would effectively be subordinated to all liabilities, including trade payables, of the subsidiary guarantors. On December 31, 2009, the subsidiary guarantors had total balance sheet liabilities of Ps. 1,237.4 million.

**The laws of New York may not be recognized in a judicial proceeding in Mexico.**

Although the choice of the laws of New York governing the notes would be recognized by the competent courts of Mexico, in the case of a dispute before a Mexican court, the Mexican court would only recognize the substantive laws of New York and would apply the laws of Mexico with respect to procedural matters. The application of any foreign law in Mexico is subject to Mexican procedural rules of evidence. Further, a Mexican court may refuse to apply and/or to enforce provisions governed by the laws of New York if the respective provision is contrary to the public policy (*orden público*) of Mexico.

## **USE OF PROCEEDS**

We intend to use the net proceeds from this offering of new notes, which are estimated to be approximately US\$192.6 million after deducting estimated underwriting discounts and offering expenses, (i) to prepay US\$105 million of the aggregate principal amount of indebtedness outstanding under our 2012 Term Loan Facility, (ii) to repay approximately US\$32 million of our short-term indebtedness under the Banamex Promissory Note, (iii) to fund approximately US\$30 million of principal installments on our indebtedness that will become due during 2010, and (iv) for general corporate purposes, capital investments and working capital requirements. See “Description of Other Indebtedness.”



## CAPITALIZATION

The following table sets forth our cash and cash equivalents and our unaudited, consolidated capitalization as of December 31, 2009, including the US\$32.0 million short-term loan incurred on January 15, 2010 under the Banamex Promissory Note, and as adjusted to give further effect to this offering, the application of the net proceeds therefrom and the use of cash as described in “Use of Proceeds.” See also “Description of Other Indebtedness.”

Our consolidated capitalization set forth below was calculated in accordance with Mexican FRS. This table should be read in conjunction with, and is qualified in its entirety by reference to, the information under the section entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations of Axtel” and our consolidated financial statements and the new notes thereto included elsewhere in this offering circular.

	As of December 31, 2009			
	Actual		As Adjusted	
	(Ps.millions)	(US\$millions)	(Ps.millions)	(US\$millions)
Cash and cash equivalents(1) . . . . .	Ps. 1,402.2	US\$ 107.4	Ps. 2,127.2	US\$ 162.9
Total debt:				
2012 Term Loan Facility USD-tranche . . . . .	329.4	25.2	—	—
2012 Term Loan Facility MXN-tranche . . . . .	1,042.4	79.8	—	—
2017 Senior Notes . . . . .	3,591.1	275.0	3,591.1	275.0
2019 Senior Unsecured Notes (including the new notes offered hereby)(2) . . . . .	3,917.6	300.0	6,398.8	490.0
Other debt and financial leases(3) . . . . .	1,389.8	106.4	971.9	74.4
Variable Fair Value Syndicated Loan(4) . . . . .	39.7	3.0	—	—
Notes premium . . . . .	—	—	62.0	4.8
Total debt . . . . .	Ps. 10,310.1	US\$ 789.5	Ps. 11,023.9	US\$ 844.2
Accrued Interest . . . . .	215.5	16.5	215.5	16.5
Total debt plus accrued interest . . . . .	10,525.6	806.0	11,239.4	860.7
Total stockholders’ equity (book value) . . . . .	8,200.9	628.0	8,200.9	628.0
Total capitalization . . . . .	Ps. 18,726.5	US\$ 1,434.0	Ps. 19,440.3	US\$1,488.7

- (1) The Company expects to enter into the 3-year New Revolving Credit Facility concurrently with or soon after the issuance of the new notes which will provide for borrowings of up to approximately US\$30 million, subject to customary terms and conditions. Currently the Company does not have plans to draw on this facility. The Company plans to use this New Revolving Credit Facility as a liquidity back-up facility that may be used in the future for general corporate purposes, capital investments and working capital requirements.
- (2) Consists of (i) US\$300.0 million aggregate principal amount of the existing notes and (ii) the US\$190.0 million aggregate principal amount of new notes offered hereby, offered at a premium of 2.5% (the premium will accrete and reduce interest expense until the new notes mature).
- (3) Includes a US\$32.0 million short-term loan incurred in January 15, 2010.
- (4) Fair value derivative financial instrument for the Company’s 2012 Term Loan terminated in connection with this offering.



## EXCHANGE RATES

As of March 8, 2010, the noon buying rate in the spot market for the purchase of U.S. dollars (in nominal pesos per U.S. dollar) was Ps. 12.6188. The following table sets forth, for the periods indicated, the period end, average, high and low noon buying rates, in each case for the purchase of U.S. dollars, all expressed in nominal pesos per U.S. dollar.

<u>Prior Years</u>	<u>Noon buying rate(1)</u>			
	<u>Period End</u>	<u>Average</u>	<u>High</u>	<u>Low</u>
Year ended December 31, 2005 .....	10.6275	10.89	11.41	10.41
Year Ended December 31, 2006 .....	10.7995	10.90	11.46	10.43
Year Ended December 31, 2007 .....	10.9169	10.93	11.27	10.67
Year Ended December 31, 2008 .....	13.8320	11.14	13.94	9.92
Year Ended December 31, 2009 .....	13.0587(2)	13.51(2)	15.37(2)	12.60(2)

(1) Federal Reserve Bank of New York.

(2) Source: Banco de Mexico.

The following table sets forth, for the periods indicated, the period end, average, high and low noon buying rates, in each case for the purchase of U.S. dollars, all expressed in nominal pesos per U.S. dollar.

<u>Month/Year</u>	<u>Noon buying rate(1)</u>	
	<u>High</u>	<u>Low</u>
January 2010 .....	13.07	12.65
February 2010 .....	13.18	12.80

(1) Source: Banco de Mexico.

Devaluation of the peso in relation to the U.S. dollar will adversely affect our ability to meet our U.S. dollar-denominated obligations, including the new notes. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations of Axtel—Liquidity and Capital Resources” and “Risk Factors—Risks Relating to Mexico—Devaluation of Mexican currency could adversely affect our financial condition.”

In the past, the Mexican economy has suffered balance of payment deficits and shortages in foreign exchange reserves. While the Mexican government does not currently restrict the ability of Mexican or foreign persons or entities to convert pesos to U.S. dollars, it has done so in the past and may do so in the future. Any such restrictive exchange control policy could adversely affect our ability to make payments in U.S. dollars, and could also have a material adverse effect on our financial condition and results of operations.

## SELECTED FINANCIAL DATA

### Axtel Selected Consolidated Financial Data

The following table provides Axtel's selected historical consolidated financial data for the fiscal years ended December 31, 2007, 2008 and 2009. We derived the selected historical consolidated financial data as of December 31, 2008 and 2009 and for the three years ended December 31, 2007, 2008, 2009 from Axtel's audited consolidated financial statements included elsewhere in this offering circular.

The information presented below should be read in conjunction with "Use of Proceeds," "Capitalization," "Management's Discussion and Analysis of Financial Condition and Results of Operations of Axtel" and the consolidated financial statements and the notes thereto included elsewhere in this offering circular.

Our financial statements have been prepared in accordance with Mexican FRS. These standards differ in certain respects from U.S. GAAP, including, but not limited to, the treatment of the capitalization of pre-operating expenses, the capitalization of interest, severance, and deferred income taxes and employees' statutory profit sharing and in the presentation of cash flow information. See "Management's Discussion and Analysis of Financial Condition and Results of Operations of Axtel—Summary of Differences between Mexican FRS and U.S. GAAP."

The figures in our audited consolidated financial statements for the years ended December 31, 2008 and 2009 and the year ended December 31, 2007 are not directly comparable given that the Company stopped recognizing inflationary effects beginning on January 1, 2008, pursuant to FRS B-10 "Inflationary Effects." See Note 3(b) and (o) and Note 4(e) to our audited consolidated financial statements for further information regarding the change with respect to inflationary accounting under Mexican FRS.

The following tables set forth selected financial data for the periods indicated, stated in nominal pesos for the years ended December 31, 2009 and 2008 and in constant pesos as of December 31, 2007 for the year ended December 31, 2007. The convenience translation exchange rate is Ps. 13.0587 per U.S. dollar.

	Year Ended December 31,			Unaudited Convenience Translation
	2007	2008	2009	Year Ended December 31, 2009
	(Millions of Ps.)			(Millions of US\$)
<b>Statement of Income Data:</b>				
Telephone services and related revenues . . . .	Ps. 12,190.6	Ps. 11,572.4	Ps. 10,968.9	US\$ 840.0
Cost of revenues and operating expenses . . . .	(10,796.8)	(10,217.8)	(10,196.1)	(780.8)
Income from operations . . . . .	1,393.8	1,354.6	772.8	59.2
Interest expense, net . . . . .	(790.6)	(742.7)	(900.7)	(69.0)
Foreign exchange gain (loss), net. . . . .	1.0	(1,602.1)	(279.8)	21.4
Change in the fair value of derivative instruments. . . . .	19.9	54.1	212.3	16.3
Monetary position . . . . .	268.8	—	—	—
Other (expense) income, net . . . . .	(20.1)	(68.4)	1.1	0.1
Income (loss) before income taxes. . . . .	872.8	(1,004.7)	365.3	28.0
Income tax (expense) benefit . . . . .	(383.2)	301.6	(181.4)	(13.9)
Equity in results of associated company . . . . .	1.4	2.8	(7.4)	(0.6)
Net income (loss) . . . . .	Ps. 491.0	Ps. (700.3)	Ps. 176.4	US\$ 13.5

	Year Ended December 31,			Unaudited Convenience Translation
	2007	2008	2009	Year Ended December 31, 2009
	(Millions of Ps., except ratios, access lines, cities and churn rate)			(Millions of US\$)
<b>Other Financial Data:</b>				
Depreciation and amortization.....	Ps. 2,690.7	Ps. 2,855.8	Ps. 3,065.8	US\$ 234.8
Investment in property, systems and equipment (fixed assets) (end of period).....	2,486.1	4,000.6	2,674.4	204.8
Net Cash Resources:				
Operating activities.....	3,226.7	2,840.9	3,449.5	264.2
Investing activities.....	(2,556.4)	(4,019.9)	(3,004.0)	(230.0)
Financing activities.....	(318.6)	(891.5)	131.0	10.0
Adjustment to cash flow from changes in foreign exchange.....	—	1,602.1	(279.8)	(21.4)
Increases (decreases) in cash or cash equivalents.....	Ps. 351.7	Ps. (468.3)	Ps. 296.7	US\$ 22.7
Adjusted EBITDA.....	Ps. 4,084.5	Ps. 4,075.3	Ps. 3,838.6	US\$ 293.9
Adjusted EBITDA Margin.....	33.5%	35.2%	35.0%	35.0%
Ratio of earnings to fixed charges(1).....	1.8x	N/A	1.3x	1.3x

**Other Data:**

Total access lines in service (in thousands) (end of period)				
Business.....	311.8	328.7	326.3	326.3
Residential.....	620.5	607.1	635.8	635.8
Total.....	932.3	935.8	962.1	962.1
Cities (end of period).....	27	39	39	39
Average Monthly Churn.....	1.6%	1.8%	1.7%	1.7%

- (1) For purposes of determining the ratio of earnings to fixed charges, earnings are defined as Axtel's income from operations before income taxes, plus fixed charges. Fixed charges consist of interest expense on all indebtedness, amortization of debt issuance costs and 33% of lease payments, which represents the amounts considered to be the interest factor of such lease payments.

	As of December 31,		Unaudited Convenience Translation
	2008	2009	As of December 31, 2009
	(Millions of Ps.)		(Millions of US\$)
<b>Balance Sheet Data:</b>			
Cash and cash equivalents.....	Ps. 1,105.6	Ps. 1,402.2	US\$ 107.4
Capital common stock.....	7,562.1	7,562.1	579.1
Total assets.....	21,569.2	21,603.1	1,654.3
Total debt.....	9,791.1	10,107.7	774.0
Total liabilities.....	13,637.7	13,402.1	1,026.3
Total stockholders' equity.....	7,931.4	8,200.9	628.0
Net Assets(1).....	14,918.6	15,507.2	1,187.5

- (1) "Net Assets" is determined by adding property, systems and equipment and net working capital investment, which is determined by subtracting from current assets, cash, income tax payable, accounts payable and other accounts payable.

## Adjusted EBITDA Reconciliation of Axtel

EBITDA is defined as net income plus net interest expense, taxes, employee statutory profit sharing, depreciation and amortization. Adjusted EBITDA is not a financial measure computed under Mexican FRS or U.S. GAAP. Adjusted EBITDA is defined as EBITDA adjusted to exclude non-recurring items and other adjustments. Axtel believes that the inclusion of supplementary adjustments to EBITDA applied in presenting Adjusted EBITDA is appropriate to provide additional information to investors about certain material non-cash and non-recurring items. Such adjustments to EBITDA may not be in accordance with current SEC practice or with regulations adopted by the SEC that apply to registration statements filed under the Securities Act and periodic reports filed under the Exchange Act. The following table reconciles EBITDA, as presented above, to net income (loss) and further reconciles Adjusted EBITDA to EBITDA.

	Year Ended December 31,			Unaudited Convenience Translation
	2007	2008	2009	Year Ended December 31, 2009
	(Millions of Ps.)			(Millions of US\$)
Net income (loss) .....	Ps. 491.0	Ps. (700.3)	Ps. 176.4	US\$ 13.5
Depreciation and Amortization .....	2,690.7	2,855.8	3,065.8	234.8
Interest expense, net .....	790.6	742.7	900.7	69.0
Income tax expense (benefit) .....	383.2	(301.6)	181.4	13.9
EBITDA .....	Ps. 4,355.5	Ps. 2,596.7	Ps. 4,324.4	US\$ 331.1
Foreign exchange (gain) loss, net. ....	(1.0)	1,602.1	(279.8)	(21.4)
Monetary position .....	(268.8)	—	—	—
Change in the fair value of derivative instruments. ....	(19.9)	(54.1)	(212.3)	(16.3)
Other expense (income), net .....	20.1	68.4	(1.1)	(0.1)
Equity in results of associated company .....	(1.4)	(2.8)	7.4	0.6
Adjustment to bad debt expense from previous years .....	—	(135.1)	—	—
Adjusted EBITDA .....	Ps. 4,084.5	Ps. 4,075.3	Ps. 3,838.6	US\$ 293.9

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS OF AXTEL

*The following discussion should be read in conjunction with the consolidated financial statements of Axtel and the new notes thereto included elsewhere in this offering circular. The following discussion includes certain forward-looking statements. For a discussion of important factors, including the continuing development of Axtel's business, actions of regulatory authorities and competitors and other factors which could cause actual results to differ materially from the results referred to in the forward-looking statements, see "Forward-Looking Statements" and "Risk Factors."*

### Overview

Axtel provides bundled local and long distance voice services, as well as data and internet services. Axtel's integrated service offering enables it to maximize the recurring revenue received from each customer, increasing the return achieved on its investment in infrastructure, sales and marketing and distribution. Long distance services, for example, have been a significant source of revenue, but would not be cost-effective to provide as a stand-alone service offering because of the significant downward pricing pressure on long distance services in Mexico. In addition, Axtel believes that customers prefer to purchase their telecommunications services from a single provider and receive a single bill. Axtel believes customer loyalty is increased with the provision of additional services, resulting in a lower customer churn rate.

### Recent Developments

On September 22, 2009, we issued US\$300.0 million of 9.0% Senior Unsecured Notes due 2019 at an issue price of 100% (the "existing notes"). We used the proceeds of the existing notes and cash on hand (i) to partially prepay the 2012 Term Loan Facility in a principal amount equal to US\$85 million, (ii) to fund the tender offer for any and all of our outstanding US\$162.5 million in aggregate principal amount of 2013 Notes at the tender offer prices, (iii) to redeem 2013 Notes that remained outstanding after the expiration of the tender offer, and (iv) for general corporate purposes, capital investments and working capital requirements. The issuance of the existing notes, the repayments of outstanding indebtedness described above are referred to collectively as the "Refinancings."

### Key Performance Indicators

Management evaluates the performance of the Company by tracking the following indicators:

	2007				2008				2009			
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
Revenues(1) . . . . .	Ps. 3,005.5	3,116.0	3,081.3	2,987.9	Ps. 2,847.4	2,933.2	2,859.1	2,932.7	Ps. 2,794.9	2,745.5	2,731.8	2,696.6
Local service . . . . .	1,278.8	1,326.1	1,337.5	1,394.3	1,291.2	1,363.9	1,340.4	1,247.0	1,174.8	1,173.8	1,181.3	1,119.5
Long distance												
Services . . . . .	402.7	419.4	352.3	357.7	332.0	341.7	319.8	292.6	307.4	305.1	297.5	278.7
Data and Network ..	619.5	628.4	645.8	620.1	618.9	618.4	616.9	646.3	640.8	632.9	585.2	593.1
International												
traffic . . . . .	293.0	330.4	313.9	272.9	238.6	228.7	182.1	333.5	298.8	310.8	368.2	346.0
Other services . . . . .	411.5	411.7	431.7	342.9	366.6	380.5	400.0	413.2	373.1	322.9	299.7	359.3
Cost of revenues and												
operating												
expenses(1) . . . . .	(2,070.8)	(2,054.7)	(1,995.2)	(1,985.4)	(1,893.8)	(1,932.7)	(1,840.5)	(1,695.0)	(1,835.1)	(1,744.0)	(1,762.9)	(1,788.3)
Access												
lines(2)(3)(4) . . . .	815.2	843.7	884.6	932.3	965.3	972.0	954.9	935.8	916.8	914.6	940.5	962.1
Average												
lines(2)(4)(5) . . . .	803.9	829.5	864.2	908.5	948.8	968.7	963.5	945.4	926.3	915.7	927.5	951.3
Monthly												
ARPU(4)(6) . . . . .	697.2	701.4	651.8	642.8	570.3	586.9	574.4	542.9	533.5	541.3	531.4	487.8
Customers(2)(3)(4) . .	518.0	543.8	576.0	623.2	659.1	667.9	654.5	639.8	626.3	625.2	654.1	681.2
Presubscription (LD)												
users(2)(3)(4) . . . .	280.8	270.0	265.1	246.1	236.1	203.1	194.4	188.6	171.4	154.3	153.8	145.9

(1) Amounts in millions of Ps.

- (2) Amounts in thousands.
- (3) Figures as of the end of each period.
- (4) Unaudited information.
- (5) Average Lines is the result of the sum of Access lines at the beginning of the period plus Access lines at the end of the period divided by 2.
- (6) Monthly ARPU is the result of the sum of local and long distance revenues divided with the Average lines of the quarter divided by 3.

### Revenues

Axtel derives its revenues from:

- *Local services.* We generate revenue by enabling our customers to originate and receive telephone calls within a defined local service area and by providing voice services bundled with Internet access for one monthly payment. Customers are charged a flat monthly fee for basic service, a per call fee for local calls (“measured service”), a per minute usage fee for calls completed on a cellular line (“calling party pays”) and value added services. Customers also acquire monthly flat fee offers, including limited or unlimited local calls, value added services and Internet access.
- *Long distance services.* We generate revenues by providing long distance services (domestic and international) for our customers’ completed calls from Axtel lines.
- *Data & network.* We generate revenues by providing data, Internet access and network services, like virtual private networks and private lines.
- *International traffic.* We generate revenues by terminating international traffic from foreign carriers.
- *Other services.* We generate revenues from other services, which include among others, activation fees, sale of customer premises equipment (“CPE”), sales and revenues generated from integrated telecommunications services provided to corporate customers, financial institutions and government entities.

The following summarizes Axtel’s revenues and percentage of revenues from operations from these sources:

Revenue Source	Revenues(1)			% of Revenues			Unaudited Convenience Translation(3) Revenues(2)
	Year Ended December 31,			Year Ended December 31,			Year Ended December 31, 2009
	2007	2008	2009	2007	2008	2009	
Local calling services . . . .	Ps. 5,336.6	Ps. 5,242.6	Ps. 4,649.5	43.8%	45.3%	42.4%	US\$ 356.0
Long distance services . . .	1,532.2	1,286.1	1,188.7	12.6%	11.1%	10.8%	91.0
Data and Network . . . . .	2,513.8	2,500.5	2,452.0	20.6%	21.6%	22.4%	187.8
International traffic . . . . .	1,210.2	982.9	1,323.8	9.9%	8.5%	12.1%	101.4
Other services . . . . .	1,597.8	1,560.3	1,355.0	13.1%	13.5%	12.3%	103.8
Total . . . . .	Ps.12,190.6	Ps.11,572.4	Ps.10,968.9	100.0%	100.0%	100.0%	US\$ 840.0

- (1) Amounts in millions of pesos.
- (2) Amounts in millions of dollars.
- (3) Convenience translation exchange rate is Ps. 13.0587 per U.S. dollar.

### *Cost of Revenues and Operating Expenses*

Axtel's costs are categorized as follows:

- Cost of revenues include expenses related to the termination of Axtel's customers' cellular and long distance calls in other carriers' networks, as well as expenses related to billing, payment processing, operator services and its leasing of private circuit links.
- Operating expenses include costs incurred in connection with general and administrative matters, including compensation and benefits, the costs of leasing land related to its operations and costs associated with sales and marketing and the maintenance of its network.
- Depreciation and amortization includes depreciation of all communications network and equipment and amortization of preoperating expenses and the cost of spectrum licenses.

### *Access Lines*

Axtel's access lines are separated into residential and business categories. Axtel determines the number of its total access lines by adding to the ending balance of access lines from the previous period the gross installed access lines during such period and then subtracting any access lines that were disconnected during such period. By then determining the number of access lines in a particular geographic market, Axtel is able to estimate its share of that market.

### *Average Revenue Per User ("ARPU")*

Average revenue per user is used as an industry-standard measurement of a telecommunications company's ability to maximize the amount of revenue it derives from each customer in light of the amount of capital expenditures made to attract such customer. This measurement allows us to gauge our return on investment as compared with both our domestic competitors in Mexico as well as other telecommunication services providers abroad. Nonetheless, sometimes lower ARPU could be explained by factors that do not necessarily imply a reduced return on investments. For example, certain technologies have capabilities to provide multiple voice lines using the same customer premises' equipment, in which case marginal revenues from the second voice line will have no incremental investment requirement but ARPU will be affected.

## **Period over Period Comparisons**

### ***Year Ended December 31, 2009 Compared with Year Ended December 31, 2008***

#### *Revenues from Operations*

Revenues from operations decreased to Ps. 10,968.9 million for the year ended December 31, 2009 from Ps. 11,572.4 million for the year ended 2008, a decrease of Ps. 603.5 million, or 5.2%. The number of access lines increased to 962,056, from 935,768, an increase of 2.8%. The decline in revenues from sales to Nextel accounts for Ps. 456.4 million, or 76%, of the total revenues decrease.

*Local services.* Local service revenues decreased to Ps. 4,649.5 million for the year ended December 31, 2009 from Ps. 5,242.6 million for the year ended December 31, 2008, a decrease of Ps. 593.1 million, or 11.3%. The decrease is explained by a reduction of Ps. 377.8 million in local service revenues from Nextel. Revenues from the rest of our customers declined Ps. 215.3 million as a result of a 3% reduction in the monthly average of lines in service, further penetration of bundled commercial offers, including calls free of charge, and lower fixed-to-mobile unit prices resulting from lower fixed-to-mobile costs.

*Long distance services.* Long distance services revenues decreased to Ps. 1,188.7 million for the year ended December 31, 2009 from Ps. 1,286.1 million for the year ended December 31, 2008, a decrease of Ps. 97.5 million, or 7.6%. The reduction is mostly explained by a decline in long distance revenues per minute from



the penetration of bundled commercial offers including packages of national and international minutes for which a monthly rent is payable and by an increase in wholesale customer traffic which carries lower unit prices.

*Data and Network.* Data and network service revenues totaled Ps. 2,452.0 million in 2009, compared to Ps. 2,500.5 million in 2008, a decrease of Ps. 48.5 million, or 1.9%, primarily explained by difficult economic conditions for business customers translating into less volume of dedicated Internet and VPN services.

*International traffic.* International traffic revenues totaled Ps. 1,323.8 million in 2009, compared to Ps. 982.9 million in 2008, an increase of Ps. 340.9 million, or 34.7%. Such increase is explained by an increase in off-net international traffic offsetting the decline in on-net international traffic.

*Other services.* Revenues from other services decreased to Ps. 1,355.0 million in the year ended December 31, 2009 from Ps. 1,560.3 million during the year ended December 31, 2008. This decrease is primarily explained by a decrease in activation fees, equipment sales, prepaid cards, special services and loyalty programs.

#### *Cost of Revenues and Operating Expenses*

*Cost of revenues.* Cost of revenues from operations decreased to Ps. 2,987.1 million for the year ended December 31, 2009 from Ps. 3,704.9 million in the year ended December 31, 2008, a decrease of Ps. 717.8 million, or 19.4%. This was due primarily to a reduction in fixed-to-mobile interconnection costs and domestic long distance costs.

*Operating expenses.* Operating expenses for the year ended December 31, 2009 increased Ps. 486.1 million to Ps. 4,143.2 million, from Ps. 3,657.1 million for the year ended December 31, 2008. Excluding the non-cash non-recurrent Ps. 135.1 million benefit recorded in the fourth quarter of 2008 as a result of a change in the uncollectable reserves accounting method for corporate customers, operating expenses would have been Ps. 3,792.2 million in 2008. The difference between the latter figure and the Ps. 4,143.2 million in operating expenses recorded in 2009 is mainly explained by increases in sales commissions generated by the acquisition of 22% more gross additional lines in 2009 compared to 2008, and increases in advertising and corporate expenses, including personnel, rents and maintenance costs. Personnel expenses increased 4.4% in 2009 compared to 2008.

*Adjusted EBITDA.* Adjusted EBITDA was Ps. 3,838.6 million for the year ended December 31, 2009 as compared to Ps. 4,075.3 million for the same period in 2008, a decrease of Ps. 236.8 million resulting from the changes in revenues, cost of revenues and operating expenses explained above. Adjusted EBITDA represented 35.0% of total revenues in the year ended December 31, 2009. See “Selected Financial Data—Adjusted EBITDA Reconciliation of Axtel.”

*Depreciation and amortization.* Depreciation and amortization increased to Ps. 3,065.8 million for the year ended December 31, 2009 from Ps. 2,855.8 million for the year ended December 31, 2008, an increase of Ps. 210.0 million, or 7.4%. The increase in depreciation and amortization reflects the company’s recent capital expenditures in 2009.

#### *Comprehensive financial results.*

The Company recorded a comprehensive financial loss of Ps. 408.7 million for the year ended December 31, 2009 compared to a Ps. 2,290.8 million loss during the year ended December 31, 2008. The reduction in the comprehensive financial loss is primarily explained by the appreciation of the Mexican peso against the U.S. dollar (compared to a significant depreciation in 2008) and by a positive variation of Ps. 87.0 million increase in the valuation of the zero-strike-calls. See “—Other financial instruments.”

The following table illustrates the comprehensive financial results comparison:

### Comprehensive Financial Result Comparison

Description	Year ended December 31,		% of Change
	2009	2008	
Interest expense(1).....	Ps. (925.3)	Ps. (801.7)	15.4%
Interest income .....	24.5	58.9	-58.4%
Foreign exchange gain (loss), net .....	279.8	(1,602.1)	N/A
Change in fair value of Derivative Instruments .....	212.3	54.1	292.7%
Total .....	Ps. (408.7)	Ps. (2,290.8)	-82.2%

(1) Interest expenses for year 2009 include Ps. 119.7 million related to the premium paid for the tender offer and early redemption of the 2013 senior notes.

#### Net Income (loss).

As a result of the foregoing factors, our net income increased Ps. 876.7 million to Ps. 176.4 million for the year ended December 31, 2009 compared to a net loss of Ps. 700.3 million recorded in the year ended on December 31, 2008.

#### Operating Data

*Lines in Service.* As of December 31, 2009, lines in service totaled 962,056, an increase of 26,288 from the same date in 2008. During 2009, gross additional lines totaled 284,902 compared to 234,201 in 2008. The number of line disconnections during 2009 was 258,614, compared to 214,264 in 2008. As of December 31, 2009, residential lines represented 66% of total lines in service. During the second half of 2009, gross additional lines totaled 176,140 compared to 111,762 in the first half of 2009. This difference is explained by the availability of competitive voice and data services through our WiMAX network, which experienced delays since 2008 until the beginning of the first quarter of 2009. The availability of competitive services offered mostly to residential and SME customers through our WiMAX network explains the increase in gross additional lines in 2009 compared to 2008. Disconnections increased by 44,350 in 2009 primarily as a result of the severe economic conditions prevailing in 2009, which affected employment and business opportunities in Mexico, increasing the number of lines disconnected due to non-payment by customers. Nonetheless, disconnections during the second half of 2009 totaled 125,661, compared to 132,953 in the first half of 2009.

*Line equivalents (E0 equivalents).* We offer dedicated data links with a capacity range from 64 kilobytes per second (“kbps”) to up to 100 megabytes per second (“Mbps”) in each of our thirty-nine existing cities. We account for data links by converting them to links with a capacity of 64 kbps per second (“E0 equivalents”) in order to standardize our comparisons versus the industry. As of December 31, 2009 line equivalents totaled 452,194, a decrease of 23,285 from the same date in 2008.

*Internet subscribers.* As of December 31, 2009, Internet subscribers totaled 174,195, an increase of 55%, from 112,223 recorded on the same date in 2008. Broadband subscribers increased 75% to 161,590 as of December 31, 2009. During 2009, broadband subscribers increased 69,269 compared to 16,629 in the same period in 2008. This significant growth is explained by our commercial efforts and the increased capacity available in our WiMAX network. Broadband additions come from new customers as well as up-selling existing subscribers from non-data or lower-speed Internet service to broadband access solutions.

## ***Year Ended December 31, 2008 Compared with Year Ended December 31, 2007***

The figures in our audited consolidated financial statements for the year ended December 31, 2008 and the year ended December 31, 2007 are not directly comparable given that the Company stopped recognizing inflationary effects beginning on January 1, 2008, pursuant to FRS B-10 “Inflationary Effects.” See Note 3(b) and (o) and Note 4 to our audited consolidated financial statements for further information regarding the change with respect to inflationary accounting under Mexican FRS.

### ***Revenues from Operations***

Revenues for 2008 were Ps. 11,572.4 million, compared to Ps. 12,190.6 million in 2007, a decrease of Ps. 618.2 million or 5.3%. The number of access lines increased to 935,768 from 932,292, a marginal increase of approximately 3,500 lines, and our average revenue per user decreased from Ps. 672 in 2007 to Ps. 568 in 2008.

*Local services.* Local service revenues for the year ended December 31, 2008, totaled Ps. 5,242.6 million, an annual decrease of Ps. 94.1 million, or 1.8%, from Ps. 5,336.6 million recorded in 2007. This change is mainly due to decreased cellular revenues per minute caused by lower fixed-to-mobile termination rates. Revenues were also affected by measured service decreases resulting from reduced local traffic.

*Long distance services.* In 2008, long distance service revenues declined to Ps. 1,286.1 million from Ps. 1,532.2 million registered in 2007, a decrease of Ps. 246.0 million, or a 16.1% decrease. Reduction in unit long distance revenues is attributable to further penetration of bundled commercial offers including packages for national and international minutes for which a monthly rent is payable.

*Data & Network.* Data and network service revenues totaled Ps. 2,500.5 million in 2008, compared to Ps. 2,513.8 million in 2007, a marginal decrease of Ps. 13.3 million, or less than 1%. The decrease is primarily explained by reduced data pricing to selected large corporate customers and federal government agencies.

*International traffic.* Revenues generated from international calls terminated in Mexico totaled Ps. 982.9 million in 2008, compared to Ps. 1,210.2 million in 2007, a decrease of Ps. 227.3 million, or 18.8%. The decline is explained by lower revenues per minute in absolute and relative terms due to the strong peso prevailing during the first nine months of 2008.

*Other services.* Revenue from other services accounted for Ps. 1,560.3 million in 2008, a decrease of Ps. 37.5 million, or 2.3%, from Ps. 1,597.8 million registered in 2007. The decline is explained by reduced activation fees caused by fewer new lines and reduced equipment sales compared with 2007.

### ***Cost of Revenues and Operating Expenses***

*Cost of Revenues.* Cost of revenues was Ps. 3,704.9 million in 2008, compared to Ps. 4,504.7 million in 2007, a decrease of Ps. 799.8 million, or 17.8%, year-over-year. This decline was mainly due to a decrease in fixed-to-mobile termination rates and domestic long distance costs.

*Operating Expenses.* In 2008, excluding the non-cash non-recurrent Ps. 135.1 million benefit recorded in the fourth quarter of 2008 as a result of a change in the uncollectable reserves accounting method for corporate customers, normalized operating expenses in 2008 would have been Ps. 3,792.2 million, compared to Ps. 3,601.4 million in 2007, an increase of Ps. 190.8 million, or 5.3%. Among others, increases of Ps. 97.2 million and Ps. 66.7 million in personnel and consulting and outsourcing (including to sales agents and access inhalation service providers) expenses, respectively, explain this growth.

*Adjusted EBITDA.* For the year ended December 31, 2008, Adjusted EBITDA amounted to Ps. 4,075.3 million, compared to Ps. 4,084.5 million in the same period in year 2007, a marginal decline of Ps. 9.2 million. Adjusted EBITDA for full-year of 2008, excludes the non-cash non-recurrent Ps. 135.1 million benefit related to our change in accounting policies relating to uncollectable reserves. See “Selected Financial Data—Adjusted EBITDA Reconciliation of Axtel.”

*Depreciation and Amortization.* Depreciation and amortization for the year ended December 31, 2008 reached Ps. 2,855.8 million, from Ps. 2,690.7 million in the same period in year 2007, an increase of Ps. 165.2 million, or 6.1%.

#### *Comprehensive Financial Results*

The Company recorded a comprehensive financial loss of Ps. 2,290.8 million for the year ended December 31, 2008 compared to a Ps. 500.9 million loss during the year ended December 31, 2007, an increase in loss of Ps. 1,789.9 million. This loss is mainly due to a 24.6% Mexican Peso devaluation from December 31, 2007 to December 31, 2008 and the effects related to the discontinuation of the recognition of inflation in accordance with Mexican FRS.

#### *Net Income (Loss)*

As a result of the foregoing factors, we reported a net loss of Ps. 700.3 million for the year ended December 31, 2008 compared to a gain of Ps. 491.0 million recorded in the year ended on December 31, 2007.

#### **Liquidity and Capital Resources**

Historically we have relied primarily on vendor financing, the proceeds of the sale of securities, internal cash from operations and the proceeds from bank debt to fund our operations, capital expenditures and working capital requirements. Although we believe that we would be able to meet our debt service obligations and fund our operating requirements in the future with cash flow from operations, we may seek additional financing in the capital markets from time to time depending on market conditions and our financial requirements. We will continue to focus on investments in property, systems and equipment (fixed assets) and working capital management, including the timely collection of accounts receivable and efficient management of accounts payable.

Net cash flows for 2009 and 2008 and resources for 2007 provided by operating activities were Ps. 3,449.5 million, Ps. 2,840.9 million and Ps. 3,226.7 million for the years ended December 31, 2009, 2008 and 2007, respectively.

Net cash flows for 2009 and 2008 and resources for 2007 used in investing activities were Ps. 3,004.0 million, Ps. 4,019.9 million and Ps. 2,556.4 million for the years ended December 31, 2009, 2008 and 2007, respectively. These amounts reflect investments in property, systems and equipment of Ps. 2,674.4 million, Ps. 4,000.6 million and Ps. 2,486.0 million for the years ended December 31, 2009, 2008 and 2007, respectively. The method used to determine cash flows from investing activities after 2007 differs from the method used for such determinations in 2007, thus the net cash flows for 2009 and 2008 may not be comparable to the net cash flow for 2007.

Net cash flows for 2009, 2008 and resources for 2007 provided by (used in) financing activities from continuing operations were Ps. 131.0, Ps. (891.5) million and Ps. (318.6) million for the years ended December 31, 2009, 2008 and 2007, respectively. The method used to determine cash flows from financing activities after 2007 differs from the method used for such determinations in 2007, thus the net cash flows for 2009 and 2008 may not be comparable to the net cash flow for 2007.

Since our inception, we have invested over Ps. 29,074.3 million in building our infrastructure. We expect to make additional investments in future years as we selectively expand our network into other areas of Mexico in order to exploit market opportunities as well as to maintain our existing network and facilities.

#### *Quantitative and qualitative market risks*

Our primary foreign currency exposure relates to our U.S. dollar denominated debt. Most of our debt obligations as of December 31, 2009 were denominated in U.S. dollars. Therefore, we are exposed to currency exchange rate risks that could significantly affect our ability to meet our obligations.

The exchange rate of the peso to the U.S. dollar is a freely floating rate and the peso has experienced significant devaluation in the previous years. Any significant decrease in the value of the peso relative to the U.S. dollar in the near term may have a material adverse effect on its results of operations and financial condition.

## Financial Instruments

### *Derivative Financial Instruments.*

The Company and its subsidiaries are exposed, by their normal business relations, to some financial risks denominated as interest rate risk and currency exchange rate risk, principally. To mitigate the exposure to those risks the Company and its subsidiaries use derivative financial instruments.

By using derivative financial instruments to hedge exposure to changes in currency exchange rate fluctuations, the Company exposes itself to credit risk and market risk. Credit risk is the risk that a counterparty fails to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes the Company, which creates credit risk for the Company. When the fair value of a derivative contract is negative, the Company owes the counterparty and, therefore, it is not exposed to credit risk. The Company minimizes the credit risk in derivative instruments by entering into transactions with high-quality foreign financial counterparties.

For derivative financial instruments that are designated as hedging activities, the Company and its subsidiaries formally document the hedging relationship, their risk management objective and strategy for undertaking the hedge, the hedging instrument, the hedged item, the nature of the risk being hedged, how the hedging instrument's effectiveness in offsetting the hedged risk will be assessed and the methodology to measure any ineffectiveness.

The Company and its subsidiaries undertake prospective and retrospective tests of effectiveness to ascertain in every moment whether the hedging employed remains effective according to applicable accounting standards. At the moment that ineffectiveness is detected, the Company registers that amount in the results as part of the comprehensive financial results ("CFR"). Due to the fact that the fair value of derivative financial instruments may suffer significant fluctuations, it is very probable that the Company will be exposed to the volatility related to unrealized profits and losses due to the changes in the fair value of derivative financial instruments in the future.

### **Derivative financial instruments with hedging purposes**

According to the accounting models for hedging activities that are permitted by financial accounting standards, the dimension, risks and estimated impact on our balance sheet or income statement of the following derivative financial instruments are presented below. In contrast to financial instruments with trading purposes, the derivatives designated as hedges will not generate volatility in our income statement, as long as the instruments are highly effective and continue to meet the financial accounting standards for hedges:

#### *Fair value hedge*

a) On March 22, 2007, the Company entered into a Currency Swap ("CCS") to cover the interest and exchange rate risk generated by the 2012 Term Loan Facility for US\$110.2 million maturing in February 2012. Under the CCS, the Company will receive payments of 3 month Libor plus 150 basis points for a notional amount of US\$110.2 million and will pay a monthly rate of TIE 28 days plus 135 basis points for a notional amount of Ps. 1,215.5 million which includes the amortizations of principal. This transaction is accounted for under the fair value hedge accounting model. During September 2009, the Company prepaid US\$85 million of the 2012 Term Loan Facility and the excess hedging position was canceled and replaced with a new cash flow hedge described below under clause (b). The CCS information is as follows:

**(Amounts in charts are expressed in millions)**

Counterpart	Notional	Conditions	Estimated fair value (USD)	
			2009	2008
Credit Suisse . . . . .	\$278 MXP \$25.2 USD	The Company pays TIE + 135 basis points and receives Libor + 150 basis points	\$3.9	\$23.3

For the year ended December 31, 2009 the change in the fair value of the hedging activity of the 2012 Term Loan Facility resulted in an unrealized loss of US\$7.0 million recognized in the comprehensive financial result, offset by the change in the fair value of the debt valued at US\$16.1 million on December 31, 2009.

*Cash flow hedge*

a) In August 2007, the Company issued US\$275.0 million senior unsecured fixed rate notes. The Company decided to enter into a new derivative to cover the risk of exchange rate derived from this issuance denominated (“Currency Swap”). Under this agreement, Axtel will receive semiannual payments calculated based on the aggregate notional amount of US\$275 million at a fixed annual rate of 7.625%, and the Company will make semiannual payments calculated based on the aggregate of Ps. 3,038.75 (nominal value) at a fixed annual rate of 8.54%.

As of December 31, 2009, the CCS information is as follows:

**(Amounts in charts are expressed in millions)**

Counterpart	Notional	Basic conditions	Estimated Fair Value (USD)	
			2009	2008
Credit Suisse . . . . .	\$3,039 MXP \$275 USD	The Company pays fixed annual rate of 8.54% and receives fixed annual rate of 7.625%	\$4.3	\$12.4

b) In September 2009, the Company entered into new derivative financial instruments. The purpose of those agreements was to hedge the debt service from the issuance of the existing notes. Under these agreements, Axtel will receive and will make payments detailed in the following table:

As of December 31, 2009, the CSS information is as follows:

**(Amounts in charts are expressed in millions)**

Counterpart	Notional	Conditions	Estimated Fair Value(USD)
			As of December 31, 2009
Credit Suisse . . . . .	\$1,623 MXP \$ 125 USD	The Company pays fixed rate in pesos of 7.696% and receives fixed rate in U.S. dollars of 9.00%	\$ 11.9
Deutsche Bank . . . . .	\$1,320 MXP \$ 100 USD	The Company pays fixed rate in pesos of 10.107% and receives fixed rate in U.S. dollars of 9.00%	(\$ 1.4)
Merrill Lynch . . . . .	\$ 658 MXP \$ 50 USD	The Company pays fixed rate in pesos of 10.0825% and receives fixed rate in U.S. dollars of 9.00%	(\$ 0.5)
Morgan Stanley . . . . .	\$ 327 MXP \$ 25 USD	The Company pays fixed rate in pesos of 10.080% and receives fixed rate in U.S. dollars of 9.00%	(\$ 0.2)

For the year ended December 31, 2009, the change in the fair value of these CCS is an unrealized gain of US\$9.52 million. This gain was recognized within the other comprehensive income section of equity, net of deferred taxes.



### *Derivatives registered as trading*

The Company only enters into financial derivative instruments intended to mitigate the risks associated with a forecasted transaction or the unpredictability of cash flows to be received or paid related to a recognized asset or liability. The Company does not speculate using financial instruments. However, the Company redeemed US\$87.5 million of its 2013 Notes on February 21, 2006. The Company did not, however, terminate the portion of the CCS attributed to that amount. As a result, the Company was over-hedged and sought to cover with an inverse CCS transaction. Pursuant to this transaction the Company received payments of 12.26% for a notional amount of Ps. 950.7 million and made payments of 11% for a notional amount of US\$87.5 million. According to Mexican FRS, this swap does not comply with the requirements of a risk hedge. However, it is considered an economic hedge by the Company. The volatility associated with this CCS was recoded in our CFR. This derivative instrument expired on December 15, 2008.

### *Embedded derivatives*

The Company has conducted an initiative to identify, analyze and segregate if applicable, those contractual terms and clauses that implicitly or explicitly embed derivatives characteristics within financial or non financial agreements. These instruments are commonly known as embedded derivatives and receive the same accounting treatment as free-standing contractual derivatives. Based on the above, the Company identified and recognized an amount of US\$0.1 million from embedded derivatives during 2009 in the accounting records.

### *Other financial instruments*

During the months of July, August and September of 2009, the Company purchased “zero strike call” options (“ZSC”) that have a notional amount equivalent to the value of 26,096,700 *Certificados de Participación Ordinarios* (“CPO”, each CPO equal to seven Series B shares) of Axtel. See Note 19(a) to our audited consolidated financial statements included elsewhere in this offering circular. Underlying these instruments is the market value of the CPOs. The price paid for the ZSCs was equivalent to the market value of the notional amount plus certain fees. The exercise price established is Ps. 0.000001 per ZSC. These instruments may be exercised only in cash. The term of these instruments is 6 months, which is renewable, and they are exercisable by us at any time before the expiration date. The position is detailed in the following table:

<u>Counterparty</u>	<u>Notional</u>	<u>Conditions</u>	<u>Fair market value</u> <u>(Millions of pesos)</u>
			<u>2009</u>
Bank of America Merrill Lynch . . . .	26,096,700 CPOs	The Company receives in cash the market value of the notional amount	\$309.5

At December 31, 2009 the change in the fair value of the ZSCs resulted in an unrealized gain of Ps. 86,911 million recognized in the CFR.



### Summary of contractual obligations

The following table discloses aggregate information about our contractual obligations as of December 31, 2009 after giving effect to the Refinancings and the issuance of the new notes and the periods in which payments are due.

<u>Contractual obligations:</u>	<u>Total</u>	<u>Less than 1 year</u>	<u>1-3 years</u>	<u>3-5 years</u>	<u>More than 5 years</u>
		(pro forma US\$ in millions)			
Debt maturing within one year .....	72.3	72.3	—	—	—
Long-term debt(1) .....	682.1	—	101.8	5.3	575.0
Interest payments(2) .....	313.9	41.9	75.3	71.2	125.5
Operating leases .....	77.3	20.1	23.4	16.5	17.3
Total contractual cash obligation .....	<u>1,145.6</u>	<u>134.3</u>	<u>200.5</u>	<u>93.0</u>	<u>717.8</u>

(1) Includes the existing notes and new notes offered hereby.

(2) Includes expected interest payments on the existing notes and the new notes offered hereby.

### Off-balance sheet arrangements.

As of December 31, 2009, the Company maintains the following stand-by letters of credit and performance and surety bonds, that due to their contingent nature, are not reflected in our balance sheet.

<u>Issuer</u>	<u>Type</u>	<u>U.S. dollars (in thousands)</u>		<u>Pesos (in thousands)</u>	
Avantel Infraestructura, S. de R.L. de C.V. ....	Leasing	US\$	0.0	Ps.	0.0
	Concession		0.0		1,363.0
	Performance		26.5		224,870.4
Avantel, S. de R.L. de C.V. ....	Leasing		0.0		0.0
	Concession		0.0		2,849.6
	Performance		0.0		157,193.4
	Other		0.0		1,515.2
Avantel, S.A. ....	Performance		0.0		10.0
	Other		0.0		529.7
Axtel, S.A.B. de C.V. ....	Leasing		0.0		464.0
	Quality		0.0		1,562.8
	Concession		0.0		1,315.2
	Performance		3.7		280,580.1
	Stand-by Letter of Credit in favor of Telmex		34,000.0		0.0
	Other		0.0		567.6
Conectividad Inalámbrica 7GHZ, S. de R.L. ....	Concession		0.0		219.2
Servicios Axtel, S.A. de C.V. ....	Others		0.0		256.6
Instalaciones y Contrataciones, S.A. de C.V. ....	Others		0.0		179.8
TOTAL .....			34,030.3		673,476.6

## Summary of Differences between Mexican FRS and U.S. GAAP

Financial statements prepared in accordance with Mexican FRS issued by the Mexican Financial Reporting Standards Board (“CINIF”) differ in certain respects from those prepared in accordance with U.S. GAAP, some of which are summarized below. The summary below does not identify all recognition, measurement, classification, presentation or disclosure differences that would affect the manner in which transactions or events are presented in our financial statements and the notes thereto. The summary below should not be considered to be exhaustive and does not include all differences between Mexican FRS and U.S. GAAP applicable to the Company. Additionally, this summary does not take into account numerous projects being undertaken by standard setting bodies in the United States that could have an impact on the comparisons between Mexican FRS and U.S. GAAP, which are applicable to us. Further, no attempt has been made to identify future differences between Mexican FRS and U.S. GAAP as a result of prescribed changes in accounting standards. Finally, no attempt has been made to identify all future differences between Mexican FRS and U.S. GAAP that may affect the Company’s financial information as a result of transactions or events that may occur in the future. In making an investment decision, investors must rely upon their own examination of the Company, the terms of the offering and Axtel’s financial information. Potential investors should consult their own professional advisors for an understanding of the differences between Mexican FRS and U.S. GAAP, and how these differences might affect the financial information herein.

### a) *Deferred taxes*

For Mexican FRS, deferred taxes are accounted for under the asset and liability method as described in the notes to the consolidated financial statements.

Under U.S. GAAP, deferred taxes are accounted under SFAS 109 “Accounting for Income Taxes,” (FASB ASC Topic 740) which uses the asset and liability method to account for deferred tax assets and liabilities. Deferred tax assets and liabilities are recognized for the future tax consequences of the differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and the tax loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax laws and rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The deferred tax effect of a change in the tax rate is recognized in the results of operations of the period in which the change is enacted. The amount of deferred taxes charged or credited to the operations in each period, for U.S. GAAP purposes, is based on the difference between the beginning and ending balances of the deferred tax assets and liabilities for each period, expressed in nominal pesos.

In assessing the materialization of deferred tax assets, companies need to consider whether it is more likely than not that some or all of the deferred tax assets will not be realized. The ultimate materialization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible.

Beginning with the adoption of FASB Interpretation No. 48 (FIN 48), *Accounting for Uncertainty in Income Taxes*, included in FASB ASC Subtopic 740-10—*Income Taxes—Overall*, as of January 1, 2009, companies recognize the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50% likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. Prior to the adoption of FIN 48, companies recognized the effect of income tax positions only if such positions were probable of being sustained.

### b) *Revenue recognition*

On December 17, 2003, the SEC issued Staff Accounting Bulletin No. 104, “Revenue Recognition in Financial Statements” (SAB 104). This bulletin summarizes the point of view of the SEC in the recognition

of revenues in the financial statements according to U.S. GAAP. The SEC concluded that only when all the following conditions are met is revenue recognition appropriate:

- a) there is persuasive evidence of an agreement;
- b) the delivery was made or the services rendered;
- c) the sales price to the purchaser is fixed or determinable; and
- d) collection is reasonably assured.

SAB 104, specifically in Topic 13A, discusses the situation of recognizing as revenue certain non-refundable up front fees. SAB 104 provides that the seller should not recognize non-refundable charges generated in certain transactions when there is continuous involvement by the vendor.

One of the examples provided by SAB 104 is activation revenues from telecommunication services. The SAB concludes that unless the charge for the activation service is an exchange for products delivered or services rendered that represent the culmination of a separate revenue-generating process, the deferral method of revenue recognition is appropriate.

Under Mexican FRS there is no specific accounting standard that addresses the matters related to revenue recognition.

**c) *Start-up costs***

In April 1998, the AICPA issued Statement of Position 98-5, "Report of Start-up Costs" (SOP 98-5), which requires start-up costs, including organization costs, to be expensed as incurred. SOP 98-5 is effective, except for certain investment companies, for fiscal years beginning after December 15, 1998. Under Mexican FRS, these costs were recognized when incurred as a deferred asset and amortized over an estimated period of time.

**d) *Allowance for post retirement benefits***

Under Mexican FRS, in accordance with FRS D-3, termination benefits for reasons other than restructuring and retirement to which employees are entitled are charged to operations each year, based on actuarial computations using the projected unit credit method. Under U.S. GAAP, post-employment benefits for former or inactive employees, excluding retirement benefits, are accounted for under the provisions of SFAS 112 and SFAS 158, which requires recognition of certain benefits, including severance, over an employee's service life.

Effective December 31, 2006, the provisions of FASB Statement No. 158 Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans (SFAS 158) is mandatory. SFAS 158 requires companies to recognize the funded or unfunded status of defined benefit pension and other postretirement plans as a net asset or liability and to recognize changes in that funded or unfunded status in the year in which the changes occur through other comprehensive income to the extent those changes are not included in the net periodic cost.

**e) *Capitalized interest***

Under Mexican FRS, companies capitalizes interest on property, systems and equipment under construction. The amount of financing cost to be capitalized is comprehensively measured in order to include properly the effects of inflation and foreign currency devaluation. Therefore, the amount capitalized includes: (i) the interest cost of the debt incurred, plus (ii) any foreign currency fluctuations that result from the related debt, and less (iii) the monetary position gain recognized on the related debt until December 31, 2007. Under U.S. GAAP, only interest is considered an additional cost of constructed assets to be capitalized and depreciated over the lives of the related assets.

**f) Supplemental cash flow information under U.S. GAAP**

Under Mexican FRS, statements of changes in financial position identify the sources and uses of resources based on the differences between beginning and ending consolidated financial statement balances in constant pesos up to December 31, 2007, and nominal pesos thereafter. Until December 31, 2007, monetary position results and unrealized foreign exchange results are treated as cash items in the determination of resources provided by operations. Under U.S. GAAP (FASB ASC Topic 230), statements of cash flows present only cash items and exclude non-cash items. The Statement of Cash Flows under US GAAP does not provide guidance with respect to inflation-adjusted financial statements. The differences between Mexican FRS and U.S. GAAP are mainly due to: (i) elimination of inflationary effects of monetary assets and liabilities from financing and investing activities against the corresponding monetary position result in operating activities, (ii) elimination of foreign exchange results from financing and investing activities against the corresponding unrealized foreign exchange result included in operating activities, and (iii) the recognition in operating, financing and investing activities of any resulted U.S. GAAP adjustments.

**g) Fair value**

On January 1, 2008, SFAS No. 157, Fair Value Measurements was effective. SFAS No. 157 (FASB ASC Topic 820) changed the definition of fair value, as defined by previous statements, to the “price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.” If market assumptions are not readily available, we use our own assumptions to reflect those that market participants would use in pricing the asset or liability at the measurement date.

SFAS No. 157 also established a hierarchy that classifies the inputs used to measure fair value. This hierarchy prioritizes the use of inputs used in valuation techniques into three levels based on observable and unobservable inputs. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of us. Unobservable inputs, which require more judgment, are those inputs described above that reflect our assumptions about the assumptions market participants would use in pricing the asset or liability, and are developed based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the reliability of inputs. If the inputs used to measure fair value fall into different levels, a disclosure is required for the item based on the lowest level input that is significant to the fair value measure.

**Recent Accounting Pronouncements**

The Mexican Board for the Research and Development of Financial Information Regulation (*Consejo Mexicano para la Investigación y Desarrollo de Normas de Información Financiera*) has issued the following Mexican FRS, effective for years beginning on or after January 1, 2010 or 2011, as indicated, and which do not provide for earlier application.

*FRS B-5 “Segment information”*

FRS B-5 is effective as of January 1, 2011. Changes as compared to superseded Bulletin B-5 “Segment Information” include the following:

- Senior management regularly discloses information by operating segment and does not require the segmentation of information into primary and secondary or into segments identified based on products or services (economic segments), geographical areas or uniform customer groups. Additionally, it requires disclosure by entity as a whole, information on its products or services, geographical areas and principal customers and suppliers).
- FRS B-5 does not require that the entity’s business areas be subject to different risks to qualify as operating segments.

- FRS B-5 allows business areas in pre-operating stage to be catalogued as operating segments.
- FRS B-5 requires disclosure by segment and separately, revenue and interest expense as well as all other components of comprehensive financial results (CFR). In specific cases, the FRS B-5 permits disclosure of net interest income.
- FRS B-5 requires disclosure of the liability amounts included in the usual operating segment information normally used by senior management in making the entity's operating decisions.

Management estimates that the initial effects of this new FRS will not be material.

#### *FRS B-9 "Interim financial reporting"*

FRS B-9 is effective as of January 1, 2010. Changes as compared to superseded Bulletin B-9 "Interim financial reporting" include the following:

- FRS B-9 requires that the interim financial information includes a comparative and condensed balance sheet, income statement, statement of stockholders' equity and statement of cash flows and, for non-profit entities, it expressly requires the presentation of a statement of activities.
- FRS B-9 establishes that the financial information at the end of an interim period should be presented comparatively with the equivalent interim period of the immediately preceding year and, in the case of the balance sheet, compared also to such financial statement at the immediately preceding year-end date.
- FRS B-9 includes and defines new terminology.

#### *FRS C-1 "Cash and cash equivalents"*

FRS C-1 supersedes Bulletin C-1 "Cash" and is effective as of January 1, 2010. The principal changes with respect to the former standard include the following:

- FRS C-1 requires the presentation of cash and cash equivalents, restricted, within the balance sheet caption of "Cash and cash equivalents".
- The term "demand temporary investments" is replaced by "available demand investments".
- To be identified as cash equivalents, the investments should be highly liquid, for example those with original maturities of three months or less when purchased.
- FRS C-1 includes the definition of the terms: acquisition cost, restricted cash and cash equivalents, highly liquid investments, net realizable value, nominal value and fair value.

Management estimates that the initial effects of this new FRS will not be material.

### **Critical Accounting Policies**

Our consolidated financial statements included elsewhere in this document have been prepared in accordance with Mexican FRS, which differ in significant respects from U.S. GAAP.

We have identified below the accounting policies we have applied under Mexican FRS that are critical to understanding our overall financial reporting.

#### *Income taxes, flat tax, and employee statutory profit sharing*

Under Mexican FRS, income taxes, flat tax and employee statutory profit sharing are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and

their respective tax bases and operating loss and tax credit carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

#### *Impairment of long-lived assets*

The Company evaluates, at least once a year, the adjusted values of its property, systems and equipment and other non-current assets subject to amortization to determine whether there is an indication of potential impairment or 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 estimated undiscounted cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed off are separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

#### *Revenue recognition*

Our revenues are recognized when earned, as follows:

- *Local calling services.* We generate revenue by enabling our customers to originate and receive an unlimited number of calls within a defined local service area. Customers are charged a flat monthly fee for basic service, a per call measured service fee, a per minute usage fee for “calling party pays” calls and a monthly fee for value-added services when requested by the customer. The costs related to the termination of our customers’ cellular in other carriers’ networks are charged to cost in the same month that the revenue is earned.
- *Long distance services.* We generate revenues by providing long distance services for our customers’ completed calls. The costs related to the termination of our customers’ long distance calls in other carriers’ networks are charged to cost in the same month that the revenue is earned.
- *Data & Network.* We generate revenues by providing Internet, data and network services, like virtual private networks and dedicated private lines. The costs related to providing Internet, data and network services to our customers are charged to cost in the same month that the revenue is earned.
- *International Traffic.* We generate revenues by terminating international traffic from foreign carriers. The costs related to the termination of international traffic are charged to cost in the same month that the revenue is earned.
- *Other Services.* We generate revenues from other services, which include among others, activation fees, equipment installation and CPEs for new customers as well as custom-made integrated telecommunications services to corporate customers.

Other costs and expenses related to sales and marketing, costs of leasing land related to our operations and maintenance of the network, billing, payment processing, operator services and our leasing of private circuit links are recorded as incurred.

#### *Estimated useful lives of plant, property and equipment*

Axtel estimates the useful lives of particular classes of plant, property and equipment in order to determine the amount of depreciation expense to be recorded in each period. Depreciation expense is a significant element of its costs, amounting to Ps. 2,777.5 million, or 27.2% of its operating costs and expenses for the year ended on December 31, 2009.

The estimates are based on historical experience with similar assets, anticipated technological changes and other factors, taking into account the practices of other telecommunications companies. We review estimated useful lives each year to determine whether they should be changed, and at times we have changed them for particular classes of assets. We may shorten the estimated useful life of an asset class in response to technological changes, changes in the market or other developments.

#### *Derivative financial instruments*

The Company accounts for derivatives and hedging activities in accordance with Bulletin C-10 for Mexican FRS, which requires that all derivative instruments be recorded on the balance sheet date at their respective fair values.

The Company uses derivative financial instruments in order to manage financial exposures, especially risks associated with foreign currency and interest rates. In accordance with FRS C-10, the Company may apply hedge accounting to such instruments if it meets certain requirements and assesses whether the derivatives that are used in hedging transactions are highly effective in offsetting cash flows of hedged items. The Company accounts for the derivative financial instruments designated as hedging activities into two main classifications: (i) fair value hedging and (ii) cash flows hedging.

In addition, the Company has accounted for certain derivative financial instruments under the classification of trade that did not meet the requirements for hedge accounting at fair value in the balance sheet, with changes in fair value recognized directly in the income statement, even though these instruments are highly effective. These derivative instruments expired on December 15, 2008.

The Company uses financial derivative instruments that are designated as a fair value hedge where the gain or loss on a derivative instrument designated and qualifying as a fair value hedging instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk shall be recognized currently in earnings in the same accounting period. For financial derivative instruments designated as a cash flow hedge the effective portion of the gain or loss on a derivative instrument designated and qualifying as a cash flow hedging instrument shall be reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged forecasted transaction affects earnings. The ineffectiveness of a gain or loss on the derivative instrument, if any, shall be recognized currently in earnings.

The ineffectiveness portion of the change in the fair value of a derivative instrument that qualifies as a hedging activity is reported in the income statement.

The Company will discontinue hedge accounting prospectively when it is determined that the derivative is no longer effective in offsetting changes in the fair value or cash flows of the hedged item, the derivative expires or is sold, terminated, or exercised. In all situations in which hedge accounting is discontinued and the derivative is retained, the Company continues to carry the derivative at its fair value on the balance sheet and recognizes any subsequent changes in the fair value of the financial instrument directly in the income statement.

On April 24, 2009, the Company created a risks committee to oversee derivative transactions in respect of notional amounts in excess of US\$30 million.

#### *Inventory*

We periodically examine our inventory in order to determine its obsolescence. Based on these examinations, we might be required to establish reserves to provide for obsolescence. To date, those circumstances have not arisen to establish such a reserve.



### *Doubtful Accounts*

In order to closely monitor our working capital accounts, we established a policy concerning our account receivable balances. For mass market and medium sized business customers, we reserve for any amount over 30 days past due. For corporate clients, we reserve for any amount over 90 days past due. For government and financial institutions, we do not create any reserve, since we have not experienced any non-payment on such accounts.

### *Use of estimates*

The preparation of consolidated financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying amount of property, systems and equipment, valuation allowances for receivables, inventories and deferred income tax assets, valuation of derivative instruments, and assets and obligations related to employee benefits. Due to the current economic environment, actual results could differ from those estimates and assumptions. Those estimates are based on the better judgment of the management of the Company. The Company's management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment which management believes to be reasonable under the circumstances. Management adjusts the assumptions when facts and circumstances dictate.

### *Contingencies*

Liabilities for loss contingencies are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. When a reasonable estimate cannot be made, qualitative disclosure is provided in the notes to the consolidated financial statements. Contingent revenues, earnings or assets, as well as employee benefits, are not recognized until their realization is virtually assured.

### *Employee benefits*

Termination benefits for reasons other than restructuring and retirement to which employees are entitled are charged to operations for each year, based on actuarial computations using the projected unit credit method. As of December 31, 2009 and for purposes of recognizing benefits upon retirement, the remaining average service life of employees entitled to plan benefits approximates 20.5 years.

## **OVERVIEW OF THE MEXICAN TELECOMMUNICATIONS INDUSTRY**

### **General**

We believe that Mexico is a unique telecommunications market in Latin America as it combines a relatively stable macroeconomic environment with a relatively low penetration of fixed lines. As a result, according to Pyramid Research Mexico's importance in Latin America's telecommunications market is expected to become more pronounced over the next four years.

Since the Mexican government initiated the liberalization of the Mexican telecommunications sector, which began with the privatization of Telmex in 1990, the Mexican telecommunications sector has become increasingly open to competition. Some of the measures implemented by the government in its liberalization process include the introduction of competition in long distance and local telephony services, the auctioning of spectrum and tariff rebalancing. The opening of the Mexican telecommunications market has created an opportunity for competitive carriers to capture market share.

### **Mexican Market Characteristics**

Mexico is the second largest country in Latin America in terms of population, with approximately 107 million people as of December 31, 2009. In addition, with a gross domestic product of US\$1,088.1 billion and gross domestic product per capita of US\$10,177 in 2008, Mexico is the second largest and one of the highest income per capita countries in Latin America. However, according to Pyramid Research, Mexico has relatively low wireline penetration compared to other countries in Latin America; with 18.3 lines per 100 inhabitants at the end of 2008. This penetration is expected to remain stable until 2012 with some participants losing market share while others, mostly new entrants, gaining or increasing market share.

### **Market Size and Projected Growth Trends**

The Mexican telecommunications services market is the second largest in Latin America in terms of revenues. Revenues from telecommunications services in Mexico, including both fixed and mobile services, are expected to grow from US\$27 billion in 2008 to US\$32 billion in 2012, a 4.6% compound annual growth rate, according to Pyramid Research.

## **MEXICAN TELECOMMUNICATIONS SERVICES MARKET GROWTH**

The fixed communications sector, which includes basic telephony, such as local and long distance voice services, and data telecommunications services, such as internet and private networks, is an important part of the Mexican telecommunications industry because of its size and the various areas of opportunity. In 2009, revenues from the fixed communications sector were approximately US\$10.2 billion. Driven by pent-up demand in data and a wider availability of services, revenues from fixed telecommunications services are expected to reach US\$9.1 billion (considering an exchange rate of Ps. 16.50 per U.S. dollar) in 2012, according to Pyramid Research.

Mobile telephony services are one of the fastest growing markets of the Mexican telecommunications industry. In 2009, revenues from the mobile communications sector were approximately US\$15.9 billion according to financial statements presented by the mobile companies. In 2009, there are approximately 83.4 million mobile subscribers in Mexico, representing the third largest penetration rate in Latin America. Pyramid Research anticipates that Mexico will continue to experience rapid growth in the number of mobile subscribers.

## **SUPERVISION AND REGULATION OF THE MEXICAN TELECOMMUNICATIONS INDUSTRY**

### **Current Regulatory Environment**

#### *General*

The telecommunications industry in Mexico is subject to the Federal Telecommunications Law and its regulations. In addition, certain rules under the General Means of Communications Law (*Ley de Vías Generales de Comunicación*) and the Telecommunications Regulations (*Reglamento de Telecomunicaciones*) remain effective.

Under the Federal Telecommunications Law, the Mexican telecommunications industry is regulated for regulatory, administrative and operational matters by COFETEL. COFETEL was created in 1996 as a separate entity from the SCT to regulate and promote the efficient development of the telecommunications industry in Mexico. COFETEL is responsible for, among other things:

- enacting regulations and technical standards for the telecommunications industry;
- ensuring that concession holders fulfill the terms and obligations of their concessions and permits;
- resolving interconnection controversies between competitors; and
- maintaining a registry of applicable rates.

The SCT retains the authority to grant and revoke all concessions and permits. COFETEL makes recommendations to the SCT on major issues, such as amending existing telecommunications legal framework, allocating spectrum frequencies, granting, transferring, renewing or revoking concessions and applying penalties for law and concession infringements. The SCT makes the final decision on these issues.

In late 2008, a new internal SCT regulation was enacted which granted certain power to the SCT which were previously held by COFETEL. We cannot predict how these new operating rules may affect our business, if at all.

#### *Concessions and permits*

To provide telephony services in Mexico through a public telecommunications network, a service provider must first obtain a concession from the SCT. Pursuant to the Federal Telecommunications Law, concessions for public telecommunications networks may not exceed a term of 30 years, and concessions for spectrum frequencies may not exceed a term of 20 years. Generally, concessions for public telecommunications networks and spectrum frequencies may be extended for a term equivalent to the term for which the concessions were originally granted as long as the concessionaire is in compliance with ongoing obligations stated therein. Concessions specify, among other things:

- the type and technical specifications of the network, system or telecommunication services that may be provided;
- the allocated spectrum frequencies, if applicable;
- the geographical region in which the holder of the concession may provide the telecommunication service;
- the required capital expenditure program;
- the term during which such service may be provided;
- the payment, where applicable, required to be made to acquire the concession, including, if applicable, the participation of the Mexican government in the revenues of the holder of the concession; and

- any other rights and obligations affecting the concession holder.

In addition to concessions, the SCT may also grant permits for the following:

- installing, operating or exploiting transmission-ground stations; and
- providing telecommunications services as a reseller.

Legally, there is no statutory maximum term mandated for these permits unless specifically stated in the permit. Under the Federal Telecommunications Law, a company needs to register with COFETEL the rates for the telecommunications services that it wishes to provide in order to be able to provide them to the public.

On March 31, 2006, the Mexican Federal Congress approved certain amendments to the Federal Television and Radio Law and the Federal Telecommunication Law, which contains certain modifications to the legal framework of the broadcasting and telecommunications industries.

In October 2006 the SCT issued a new convergence program by which the concessionaires of telephony services are allowed to provide paid television and audio services and the concessionaires of paid television and audio services are allowed to provide telephony services as long as the concessionaires adhere and accept the program's terms, which include among others, the obligation to allow telephone number portability.

*Ownership restrictions.* Under the Federal Telecommunications Law and the Mexican Foreign Investment Law (*Ley Federal de Inversión Extranjera*), basic telephony concessions may be granted only to:

- Mexican individuals; and
- Mexican corporations in which non-Mexicans own 49% or less of the full voting stock and that are not otherwise controlled by non-Mexicans.

However, in the case of concessions for cellular telecommunications services, foreign investment participation may exceed 49% of the voting stock with the prior approval of the Mexican Foreign Investment Bureau of the Mexican Ministry of Economy (*Secretaría de Economía*).

Pursuant to the Foreign Investment Law, the Mexican Ministry of Economy may also authorize the issuance of non-voting or limited-voting stock (also known as "neutral shares") that are not counted for purposes of determining the foreign investment percentage of a Mexican corporation under the Mexican Foreign Investment Law. Any share transfers resulting in a violation of these foreign ownership requirements are invalid under Mexican law.

*Transfer.* Concessions are transferable three years after the concession is granted. If the SCT approves the transfer of the concession title, the assignee agrees to comply with the terms of the concession and such a transfer does not violate the foreign ownership requirements of the Federal Telecommunications Law and the Mexican Foreign Investment Law.

*Termination.* A concession or a permit may be terminated pursuant to the Federal Telecommunications Law upon the following events:

- expiration of its term;
- resignation by the concession holder or the permit holder;
- dissolution or bankruptcy of the concession holder or the permit holder; or
- revocation by SCT.

*Revocation.* A concession or a permit may be revoked pursuant to the Federal Telecommunications Law upon the following events:

- failure to exercise the rights of the concession within 180 days of its granting;
- failure to provide interconnection services with other holders of telecommunications concessions and permits without just cause;
- loss of the concession or permit holder's Mexican nationality;
- unauthorized assignment, transfer or encumbrance of the concession or permit;
- unauthorized interruption of service;
- taking any action that impairs the rights of other concessionaires or permit holders;
- failure to comply with the obligations or conditions specified in the concession or permit; and
- failure to pay the Mexican government its fee for the concession or, where applicable, its participation in the revenues of the holder of the concession.

The SCT may revoke a concession for violations in any of the circumstances referred to in the first four instances above. Under the last four instances above, the SCT would have to sanction the concessionaire at least three times for these failures before revoking a concession.

#### *Expropriation*

The Mexican government has the statutory right to permanently expropriate any telecommunications concession and claim any related assets for reasons of public interest. Under Mexican law, the Mexican government is obligated to compensate the owner of such assets in the case of a statutory expropriation. The amount of the compensation is to be determined by appraisers. If the party affected by the expropriation disagrees with the appraisal amount, such party may initiate judicial action against the government. In such a case, the relevant judicial authority will determine the appropriate amount of compensation to be paid. We are not aware of any instance in which the SCT has exercised its expropriation rights in connection with a telecommunications company.

#### *Temporary seizure*

The Mexican government, through the SCT, may also temporarily seize all assets related to a telecommunications concession or permit in the event of a natural disaster, war, significant public disturbance, threats to internal peace or for economic reasons or for other reasons related to national security. If the Mexican government temporarily seizes such assets, except in the event of war, it must indemnify the concession holder for all losses and damages, including lost revenues. We are not aware of any instance in which the SCT has exercised its temporary seizure attributions in connection with a fixed or mobile telecommunications services company.

#### *Rates for telecommunications services*

Before the Federal Telecommunications Law was enacted, the SCT's approval was required for setting the rates charged for all basic local, long distance and certain value-added local and long distance telecommunications services. Historically, the SCT permitted rate increases based on the cost of service, the level of competition, the financial situation of the carrier and certain macroeconomic factors. Carriers were not allowed to discount the rates authorized by the SCT, although operators occasionally waived activation fees on a promotional basis. Interconnection rates also required SCT approval. Rates for private dedicated circuit services through microwave networks and private networks through satellites were not regulated before the Federal Telecommunications Law was enacted.

Under the Federal Telecommunications Law, rates for telecommunications services (including local, cellular and long distance telephony services) are now freely determined by the providers of such services, except that such rates may not be set below a service provider's long-term incremental cost.

In addition, COFETEL is authorized to impose specific rate, quality and service requirements on those companies determined by the CFC to have substantial market power pursuant to the provisions of Mexico's antitrust statute. All rates for telecommunications services (other than value-added services) must be registered with COFETEL prior to becoming effective. The Federal Telecommunications Law prohibits telecommunications providers from cross-subsidizing among their services and requires that they keep separate accounting for each of their services.

Recently, in July 2009, the Mexican Antitrust Commission has found that Telmex has substantial power in the following markets: wholesale local, national and international long distance, cross border and interconnection circuit leasing services and local transit of voice traffic through networks that render local fixed service, as defined under Mexico's antitrust statute. Based on this finding, COFETEL may impose special obligations on Telmex regarding, among other things, quality of services, tariffs and information disclosure on these markets. However, Telmex is on time to dispute these resolutions, therefore we are not certain that they will be applied.

#### *Tax law*

In accordance with the current tax legislation, companies must pay the greater of Income Tax (IT) or Flat Tax (IETU) beginning on 2008 (or Asset Tax (AT) in 2007 and 2006). The IT rate in Mexico was 28% for 2009. Beginning on January 1, 2010, the IT rate will be 30% from 2010 to 2012, 29% for 2013 and 28% for 2014 and thereafter. Mexican regulations allow companies to deduct tax losses against taxable income, potentially reducing tax payments. If IETU is payable, the payment will be considered final and not subject to recovery in subsequent years. The IETU rate is 17% for 2009 and 17.5% for 2010 and thereafter. All of the taxes recognize the effects of inflation but in a manner different from financial reporting standards.

## BUSINESS

### Our Company

We are the second-largest, and one of the fastest growing, fixed-line, integrated telecommunications companies in Mexico, measured in revenues, EBITDA and lines in service. We offer a wide array of services, including local and long distance telephony, broadband Internet, data and built-to-suit communications solutions in 39 cities and long distance telephone in close to 200 cities to more than 827,000 business and residential customers. In 2009, we generated revenues and operating income of Ps. 10,968.9 million (US\$840.0 million) and Ps. 772.8 million (US\$59.2 million), respectively.

We provide services using a hybrid wireline and fixed wireless local access network (including 1,562 kilometers of metro fiber optic rings) along with approximately 7,700 kilometers of long-haul fiber-optic network. As of December 31, 2009 our last-mile access, designed to optimize capital expenditures through the deployment of network access equipment based on specific customer requirements, includes 57 digital switches, 433 proximity access sites, 155 symmetry access sites, 573 WiMAX access sites, 254 point-to-multipoint sites and 3,103 point-to-point links. Our nationwide long-haul network includes approximately 7,700 kilometers of fiber optic network with links to terminate long distance traffic in close to 200 cities as of December 31, 2009. As of December 31, 2009, we have invested in the aggregate approximately Ps. 29,074.3 million in network and infrastructure.

Our strategy is to continue to penetrate our existing markets by offering a comprehensive portfolio of high quality, facilities-based voice, data, internet, integrated solutions and value-added communications services and to cost-effectively enter into selective new markets with high growth and revenue opportunity. Our approach is to bundle multiple voice, data and Internet services into integrated telecommunications solutions for businesses and high-usage residential customers. We also intend to continue servicing foreign carriers with international traffic termination, as well as providing custom-made integrated telecommunications services to large corporate customers. For the year ended December 31, 2009, approximately 79% of our revenues were generated from business customers and 21% from residential customers. Axtel was founded in 1994 and in June 1996 was awarded by the Mexican government a concession to install and operate a public telecommunications network for the offering of local and long distance telephony services in Mexico. On December 4, 2006, Axtel acquired Avantel, adding an IP-based nationwide telecommunications network. Due to the acquisition, we now hold the following spectrum assets: two concessions at 929 MHz for radio-messaging services, 56 MHz at 7 GHz for nationwide long-haul point to point transport, 60 MHz at 10.5 GHz in three regions and 60 MHz at 10.5 GHz nationwide for point to multi-point access; 168 MHz at 15 GHz, 368 MHz at 23 GHz for nationwide point to point transport and 112 MHz at 37 to 38.6 GHz in five regions.

On September 15, 2009, Mexico's Ministry of Communications and Transportation granted us a concession to provide direct-to-home ("DTH"), or satellite-TV, video services in Mexico. As a result of obtaining this concession, we believe Axtel will be able to set up its DTH infrastructure and offer voice, internet and video services together, which will enable us to compete more effectively in the residential segment, particularly with triple-play offers from cable companies. See "—Products and Services."

We provide local, long distance, data, internet, integrated solutions and value-added communications services in 39 of the largest metropolitan areas in the country, including Mexico City, Monterrey, Guadalajara, Puebla, Toluca, León, Querétaro, San Luis Potosí, Saltillo, Aguascalientes, Ciudad Juárez, Tijuana, Torreón (Laguna Region), Veracruz, Chihuahua, Celaya, Irapuato, Cd. Victoria, Reynosa, Tampico, Cuernavaca, Merida, Morelia, Pachuca, Hermosillo, San Juan del Rio, Xalapa, Durango, Villahermosa, Acapulco, Mexicali, Cancun, Zacatecas, Matamoros, Nuevo Laredo, Culiacan, Mazatlan, Coatzacoalcos and Minatilan. These 39 cities represent 46.4% of the total population of Mexico according to Mexico's Instituto Nacional de Estadística Geografía e Informática, INEGI. We estimate that our total lines represent approximately 9.7% of the lines in service of our total addressable market in the 39 cities in which we provide local services. Additionally, our long-haul network provides long distance and data services in close to 200 cities across the country. We expect our



growth will come from both continued customer acquisitions and the build out of our network within our current markets and in selected new cities as we continue to expand our coverage and capacity in the major metropolitan areas of Mexico.

In December 2007, we entered into an agreement with Motorola de Mexico S.A. de C.V. and Motorola Inc. to integrate WiMAX technology into AXTEL's Network. Additionally, we signed an agreement with the CFE to have access to their extensive fiber optic network and increase our capacity of provisioning private line and data services in the country.

*Market Size and Projected Growth Trends.* Mexico is the second largest country in Latin America in terms of population, with approximately 107 million people as of December 31, 2009, and a gross domestic product of US\$1,088.1 billion and a gross domestic product per capita of US\$10,177 as of December 31, 2008. According to Pyramid Research, Mexico has relatively low wireline penetration compared to other countries in Latin America; with 18.3 lines per 100 inhabitants at the end of 2008. This penetration is expected to remain stable until 2012 with some participants losing market share while others, mostly competitive local exchange carriers, gain or increase market share. The fixed communications sector, which includes basic telephony, such as local and long distance voice services, and data telecommunications services, such as internet and private virtual networks, is an important part of the Mexican telecommunications industry because of its size and growth opportunity. In 2009, revenues from the fixed communications sector were approximately US\$10.2 billion.

*Favorable Regulatory Environment.* The Mexican telecommunications market has long been dominated by Teléfonos de Mexico, S.A.B. de C.V. ("Telmex"), the former government-owned telecommunications monopoly. Since the Mexican government completed the privatization of Telmex in 1990, the Mexican telecommunications sector has become increasingly open to competition. The opening of the Mexican telecommunications market has created an opportunity for competitive carriers to capture market share from Telmex. As the owner and operator of a network servicing Mexico's largest metropolitan markets, we believe we are well positioned to continue to take advantage of this market opportunity.

## **Competitive Strengths**

*Leading Market Position.* As one of the first competitive providers to approach customers with bundled local, long distance voice and data services in a significant number of cities across the country, we believe that we are able to meet pent-up demand for an alternative service provider and establish brand awareness and customer relationships prior to market entry by emerging competitors. We have benefited from our "first-competitor-to-market" advantage by capturing what we estimate to be approximately a 9.7% share of our total addressable market in the 39 cities where we offer local services as of December 31, 2009. In Monterrey and Guadalajara, the first two markets where Axtel launched operations in 1999, we estimate that as of December 31, 2009 we have a market share of approximately 15% and 13%, respectively.

*Comprehensive Voice and Data Service Portfolio.* We provide our customers an integrated bundle of services that includes local and long distance voice services, as well as internet, data and other value-added services. We believe our comprehensive service portfolio enables us to build strong, long-term relationships with customers and increase our return on our investment in network infrastructure. Furthermore, our digital access, transport and innovative last-mile technologies enable us to meet the growing demand for data services.

*Scalable Digital Network.* Our hybrid fixed wireless and wireline local access network structure allows us to enter new markets quickly and cost-effectively. By utilizing the fixed wireless access technology model, we are able to quickly cover a substantial geographic area with reduced initial capital expenditures. We defer most incremental capital expenditures for last-mile connectivity until the customer subscribes to our service. As of December 31, 2009, our network consisted of 57 digital switches, 433 Proximity access sites, 155 Symmetry access sites, 573 WiMAX access sites, 254 point-to-multipoint sites, 3,103 point-to-point links and 1,562

kilometers of metropolitan fiber optic rings. As of December 31, 2009, we have invested in the aggregate approximately Ps. 29,074.3 million in network and infrastructure to build an extensive local and national telecommunications network.

*Flexible and Innovative Technology.* Our ability to add new last-mile technologies allows us to continuously satisfy the changing requirements of existing and new customers. The deployment of 802.16e WiMAX, a new IP-based voice and data wireless technology designed to deliver voice and data solutions, under fixed, portable, nomadic and mobile environments, increases our ability to provide high-quality voice and data access solutions. We have initiated the gradual conversion of selected coverage clusters from wireless technologies to fiber. Such conversion will enhance our ability to provide integrated data, voice and video services. The conversion criteria are based on existing customer density and potential business opportunities. A significant portion of the existing wireless technologies can be re-deployed to other areas.

*Scale—Second-Largest Fixed-Line Integrated Telecommunications Company in Mexico.* We are the second largest local, national and international long distance and data services provider in Mexico, measured in lines in service, revenues and EBITDA. The size of our operations enables us to benefit from economies of scale.

*Favorable Financial Profile.* We have favorable Adjusted EBITDA generation (Ps. 3,838.6 million in 2009 and Ps. 4,075.3 million in 2008) and financial ratios with net debt to Adjusted EBITDA of 2.3x and 2.1x for each of the years ended on December 31, 2009 and December 31, 2008, respectively, and Adjusted EBITDA to net interest expense of 4.8x for the year ended December 31, 2009, excluding the premium paid for the tender offer and early redemption of the 2013 Notes, and 5.1x for the year ended December 31, 2008.

*Experienced Management Team and Internationally Renowned Equity Partners.* Our senior management team has extensive entrepreneurial, financial, marketing and telecommunications expertise. The diverse experience of our senior management team has contributed significantly to our initial success and rapid growth. In addition, we have benefited from working currently and in the past with strong local partners and experienced multinational investors such as The Blackstone Group, Citigroup Inc. and AIG-GE's Latin American Infrastructure Fund. Our local investors and directors include, among others, Tomás Milmo Santos, Thomas Milmo Zambrano, Alberto Santos de Hoyos, Lorenzo Zambrano Treviño and senior executives from Banamex. These investors have extensive financial, operating and senior management experience in large Mexican corporations.

## **Strategy**

The key elements of our business strategy are:

*Target Service Sectors with High Profitability Potential.* We have divided our target market into the business market and residential market. Within the business market, we address the needs of micro and small business as well as medium and large companies, multinationals, financial institutions and government entities. We have developed differentiated, targeted telecommunications services plans designed to capture business and retain high-usage customers in each market. In the residential market, we focus on high-usage customers. We believe that by focusing on the business and high-usage residential customers within a coverage area we are able to increase the return per dollar invested in our network infrastructure. For the year ended December 31, 2009, approximately 79% of our revenues were generated from business customers and 21% from residential customers.

*Bundle Products in an Integrated Offering.* We believe that the bundling of voice, data and internet services into communications solutions for our customers enables us to generate higher revenue per customer and more revenue per dollar invested in access infrastructure while also generating customer loyalty. We have focused and will continue to focus on increasing the penetration of bundled products to our customer base. By being a facilities-based telecommunications service provider, we believe we are well positioned to offer our customers the convenience of receiving voice, data and internet services from a single provider. For corporate customers, financial institutions and government entities, we offer integrated solutions based on the specific needs of the

customers, including design, implementation, maintenance and monitoring of their networks. For medium-size clients, we bundle voice and data packages that specifically meet their requirements in a cost-efficient way.

*Maintain Voice Revenues Stream.* Although the data market represents an attractive and expanding revenues opportunity compared to slow growing voice-related revenues, over 70% of Mexican telecommunications industry revenues in 2009 are voice related. A significant voice revenue stream provides the leverage to further penetrate the fast-growing data market. Therefore, we will continue to strive to maintain a stable voice revenue stream.

*Focus on Customer Service and Retention.* Since launching operations, we have been focused on achieving customer satisfaction levels that are superior to the incumbent and our primary competitors. We believe that our service-driven customer care leads to superior customer satisfaction, which enhances profitability and cash flow by increasing customer retention and expanding sales opportunities.

*Continue to Expand Technologically Advanced Network Infrastructure.* We continuously evaluate opportunities for network expansion both within our existing cities and additional regions in order to enhance our coverage area. We believe that selectively expanding our network and coverage area will enhance our ability to acquire large business customers with multi-city operations, which we expect will result in higher revenues and margin improvements while minimizing capital expenditures. We may also expand our network or operations through acquisitions or strategic agreements, as we believe there may be additional opportunities for consolidation in the Mexican telecommunications industry. We are not currently engaged in formal negotiations with any company regarding a potential acquisition or strategic agreement but may engage in conversations with third parties from time to time regarding strategic acquisitions or combinations.

## **Products and Services**

We offer a wide variety of telecommunications services, including, local, long distance, Internet, and data services, such as virtual private lines, dedicated private lines, frame relay and web-hosting. We also provide integrated telecommunications services such as network monitoring, call center outsourcing and LAN design, operation and maintenance services.

The Company's revenues are derived from (a) customers' use of our integrated network with central and local infrastructure and (b) commercial activities including provision of services and selling customer premises equipment. The Company generates revenues from customers' utilization of our integrated network ubiquitously utilizing the same physical assets and operating under the same concessions. Significant resources are allocated to the network on a total enterprise basis, without consideration of specific geographic areas. Expenses incurred, are also incurred on a total enterprise basis. Therefore, the Company does not analyze its financial information on the basis of geographic market. To analyze revenues, the Company tracks the following five categories:

(i) *Local services:* We generate revenues by enabling our customers to originate and receive an unlimited number of calls within a defined local service area. Customers are charged a flat monthly fee for basic service, a per call measured service fee, a per minute usage fee for "calling party pays" calls and a monthly fee for value added services.

(ii) *Long distance services:* We generate revenues by providing long distance services for our customers' completed calls.

(iii) *Data and private lines:* We generate revenues by providing Internet, data and network services, such as virtual private networks and dedicated private lines.

(iv) *International traffic:* We generate revenues by terminating international traffic from foreign carriers.

(v) *Other services:* We generate revenues from other services such as activation fees, from the sale and/or lease of customer premises equipment for new customers and custom-made integrated telecommunications services to corporate customers.

We offer the following products and services:

**Voice**

- Business and Residential Line
- Long Distance
- Digital Trunks
- Voicemail
- Centrex Line
- Customer Premise Equipment
- Telephone Sets, Key Systems and PBX
- Call Waiting, Call Forwarding, Caller ID, Conference Call
- Directory Assistance
- Operator Services
- Automatic Dialing
- Unique number
- Prepaid Services
- Collect Calls
- Virtual Line
- Toll Free Services

**Bundles:**

- Axtel in a Box
- Axtel Libre Hogar Internet
- Axtel x2
- Axtel Libre Hogar Total

**Data**

- Local and Domestic Private Lines
- High Speed Private Lines
- Co-location
- Virtual Private Networks (MPLS)

**Internet**

- Dial Up Internet
- Dedicated Internet
- Web Hosting
- Internet on Demand
- Internet FWA
- Co-location

**Integrated Services:**

- Data Centers
- Network Monitoring
- Contact Centers
- Network Security Monitoring
- LAN Maintenance
- LAN Design and Operation

With our DTH concession, we expect to combine data and voice services with video solutions, which we believe will strengthen our competitive position in the residential segment. We expect to offer a variety of video services, ranging from entry level packages to premium content offers and providing both national and international content. We believe our video services subscribers, which will be primarily residential customers, will benefit from better pricing by acquiring voice, data and video services from Axtel.

**Our Markets**

We provide local, long distance, data, internet, integrated solutions and value-added communications services in 39 of the largest metropolitan areas in the country, including Mexico City, Monterrey, Guadalajara, Puebla, Toluca, León, Querétaro, San Luis Potosí, Saltillo, Aguascalientes, Ciudad Juárez, Tijuana, Torreón (Laguna Region), Veracruz, Chihuahua, Celaya, Irapuato, Ciudad Victoria, Reynosa, Tampico, Cuernavaca, Mérida, Morelia, Pachuca, Hermosillo, San Juan del Rio Xalapa, Durango, Villahermosa, Acapulco, Mexicali, Cancun, Zacatecas, Matamoros, Nuevo Laredo, Culiacan, Mazatlan, Coatzacoalcos and Minatilan. These 39 cities represent 46.4% of the total population of Mexico according to INEGI. With our long-haul network we also provide long distance services in close to 200 cities in Mexico. We estimate that the cities in which we operate locally represent the majority of the total Mexican telecommunications revenue opportunity.

Our city roll-out is determined taking into consideration the following criteria:

- *Size of telecommunications opportunity.* According to COFETEL, as of December 31, 2009, approximately 60% of the total fixed lines in Mexico were concentrated in 7 of the 32 states: State of Mexico, Jalisco, Nuevo Leon, Puebla, Distrito Federal, Veracruz, and Guanajuato. Twelve of the 39 cities we currently serve are in these states and six of them are state capitals.

- *Regional economy.* According to INEGI, in 2007, almost 89% of the total gross domestic product in Mexico was generated in the 25 states in which we have a local presence.
- *Operational synergies.* To become more efficient in launching cities, we decided to open clusters of cities to allow for quick systems and operations integration and network build-out.

Within these cities, studies were conducted using geographical, statistical and self-generated market research data to determine where the most attractive opportunities were concentrated. Our network has been built upon this comprehensive data allowing for fast penetration and cost-efficiency.

We believe that as of December 31, 2009 we have a 9.7% market share of our total addressable market in the 39 cities in which we offer local services. In Monterrey and Guadalajara, the first two markets where Axtel launched services, we estimate that we have achieved market shares, in each city, of approximately 15% and 13%, respectively. In particular, in the business market, we estimate that in Monterrey and Guadalajara we have achieved approximately a 18.8% and 23.3% market share, respectively. The table below provides our estimated market share as of December 31, 2009 for each of the cities where we offer local services, based on access lines.

**Market Share Within Coverage Market  
As of December 31, 2009**

<u>City</u>	<u>Date Launched</u>	<u>Residential</u>	<u>Business</u>	<u>Total</u>
Monterrey . . . . .	Jun-99	13.0%	18.8%	14.5%
Guadalajara . . . . .	Dec-99	10.2%	23.3%	13.0%
Mexico . . . . .	Mar-00	6.8%	13.8%	8.7%
Leon . . . . .	Jan-01	7.8%	18.1%	9.7%
Puebla . . . . .	Jan-01	8.5%	11.7%	9.4%
Toluca . . . . .	Jan-01	9.1%	11.3%	9.6%
Queretaro . . . . .	Jul-04	7.0%	10.6%	7.9%
San Luis Potosi . . . . .	Jul-04	16.7%	19.6%	17.4%
Aguascalientes . . . . .	Oct-04	11.4%	12.0%	11.5%
Saltillo . . . . .	Oct-04	11.2%	16.3%	12.2%
Ciudad Juarez . . . . .	Nov-04	8.0%	11.5%	8.7%
Tijuana . . . . .	Nov-04	4.2%	4.4%	4.3%
Torreon . . . . .	Feb-06	10.3%	13.1%	10.9%
Veracruz . . . . .	Feb-06	12.1%	10.1%	11.7%
Chihuahua . . . . .	Mar-06	7.3%	9.9%	7.8%
Celaya . . . . .	May-06	11.4%	9.4%	11.0%
Irapuato . . . . .	Aug-06	11.2%	8.7%	10.8%
Cuernavaca . . . . .	Mar-07	13.5%	9.3%	12.5%
Tampico . . . . .	Mar-07	15.4%	15.6%	15.4%
Morelia . . . . .	May-07	12.6%	7.9%	11.5%
Mérida . . . . .	Jun-07	6.7%	4.4%	6.2%
Xalapa . . . . .	Jun-07	11.7%	12.8%	11.9%
Hermosillo . . . . .	Aug-07	5.0%	5.6%	5.1%
Victoria . . . . .	Oct-07	15.0%	11.5%	14.2%
Pachuca . . . . .	Oct-07	12.2%	10.7%	11.9%
Reynosa . . . . .	Oct-07	10.1%	7.7%	9.6%
San Juan del Rio . . . . .	Oct-07	14.4%	13.3%	14.2%
Coatzacoalcos . . . . .	Jun-08	11.2%	6.1%	10.1%
Culiacán . . . . .	Jun-08	3.1%	6.8%	4.0%
Matamoros . . . . .	Jun-08	11.2%	4.6%	9.6%
Mazatlán . . . . .	Jun-08	4.0%	2.9%	3.7%

<u>City</u>	<u>Date Launched</u>	<u>Residential</u>	<u>Business</u>	<u>Total</u>
Minatitlán .....	Jun-08	9.1%	3.2%	7.8%
Nuevo Laredo.....	Jun-08	14.2%	3.0%	11.2%
Acapulco.....	Dec-08	4.4%	3.3%	4.2%
Cancun.....	Dec-08	5.6%	2.4%	4.6%
Durango.....	Dec-08	6.3%	4.9%	6.1%
Mexicali .....	Dec-08	4.9%	2.6%	4.3%
Villahermosa .....	Dec-08	3.9%	2.7%	3.6%
Zacatecas.....	Dec-08	5.1%	4.8%	5.0%
<b>Total .....</b>		<b>8.5%</b>	<b>13.2%</b>	<b>9.7%</b>

Source: Market share percentages are company estimates based on number of lines in service divided by the average teledensity per square kilometer of coverage for each one of our radiobases.

Banamex, and its Mexican affiliates, Verizon Communications (formerly MCI) and Nextel de Mexico, represent 22% of our total revenues as of December 31, 2009. We signed a five-year contract with Banamex on November 27, 2006, renewable for another five years, to provide products and services for all their telecommunications needs in existing and new operations. Verizon Communications provides us a significant volume of international traffic that terminates in Mexico, representing 5% of our total revenues for 2009. Additionally, we invoiced 4% of our total revenues to Verizon for services rendered to Verizon’s global customers in Mexico in 2009. We have maintained this relationship with Verizon Communications since 1995. Nextel de Mexico provides telecommunications services to some of its customers through access to our network. We first entered into a services agreement with Nextel de Mexico in April 2001, and this agreement has been extended eight times. Pursuant to this business relationship, we extended the agreement until August 31, 2011 to continue providing Nextel de Mexico with local services, spectrum, long distance and 01-800 numbers, and other services, in a significant number of Mexican cities. Under this extension, Nextel de Mexico will gradually exclude certain geographic areas, and the respective traffic or volume, from the agreement every year, therefore gradually reducing the contribution of Nextel de Mexico in the Company’s revenues.

Our telecommunications business is susceptible to seasonality, where our volume related revenues are impacted due to lower consumption levels in vacation and holiday periods. We estimate that as of December 31, 2009 approximately 25% to 35% of our revenues are volume related.

## **Marketing and Sales**

Our marketing strategy is to position ourselves as the first and best alternative provider of local, long distance, internet, data and value-added integrated telecommunications services in Mexico. We undertake direct mail marketing (both special delivery and bill inserts) as well as telemarketing in order to generate geographically targeted brand awareness and to up-sell new services to existing customers. We also build brand awareness through the use of outdoor advertising and billboards, printed media including newspapers and magazines, advertisements on the radio and television and sponsorships of local news programs and co-sponsorship of programs with important companies in Mexico. Our brand strategy is to convey a modern, attractive image using simple, visual communication and portraying a human profile.

For corporate customers, financial institutions and federal government entities, we launched “*AXTEL Corporativos*,” a marketing initiative to strengthen our position as a unified communications supplier with a broad range of administered solutions that allow large customers to increase the efficiency of their communications by converging different services. This group is responsible for all sales activities, contract negotiations and proactive account management.

We complement this marketing campaign with focused sales efforts directed to our target market using a variety of sales channels. Our primary sales methods are: direct sales; door to door sales; telemarketing; sales



booths in strategically determined areas, including department stores, where potential customers carry out their shopping activities; MAPs (“*Módulos de Atención y Pago*”), which are Axtel-branded sales and service offices located at strategic locations within our targeted cities; and sales distributors who are certified to carry out sales activities on our behalf and target specific niches.

Sales efficiency is measured by subscriber acquisition cost. Telemarketing has proven to be a highly efficient sales channel due to the quality of our detailed database systems, which screen potential customers based on geographic location, network availability and expressed interest. By effectively pre-selecting customers based on network availability, we are able to maximize telemarketing sales efficiency and decrease the cost of acquisition. The accuracy of our databases also results in highly efficient installations.

Customer churn occurs primarily from our disconnecting customers for non-payment of bills. Churn also occurs when a customer chooses to switch to a competing service or to terminate service altogether. Churn results in the loss of future revenue from customers whose service is disconnected and limits our ability to recoup costs incurred in acquiring customers such as switching costs, commissions and installation costs. Our average monthly churn rate for the year ended December 31, 2009 was 1.7%% compared to 1.8% for the same period in 2008.

## **Pricing**

In the residential market, in order to attract new subscribers, we actively promote attractive packages or bundles, which generate recurring monthly payments, like *Acceso Universal* packages, which may include unlimited local calls, domestic and U.S. long distance minutes and broadband Internet access to mass market customers. Once a customer has chosen our services, we focus on customer satisfaction and offer the customer benefits, rather than lower pricing, in order to maximize our retention rate. For instance, under the Axtel x 2 program we install and activate second lines for a small charge and allow customers free service trials for value-added services. In the business market, we attract users by offering a wide variety of advanced telecommunications services, like VPNs, dedicated private lines, co-location and network monitoring, in addition to voice services, which differentiate us from most of our competitors. For voice products, we offer volume discounts on local calls and provide additional services and discounts to customers who sign long-term contracts. To date, this strategy has allowed us to capture significant market share without eroding the value of the market through excessive price competition.

We maintain our prices at market levels. We offer pricing plans that are simple in order to assure customers of the integrity of the billing process. Our pricing structure rewards consumption by increasing discounts in relation to the amount billed. Our ability to introduce new products such as Axtel Libre Hogar Local, or Axtel Libre Hogar Internet, allows us to position ourselves as a value-added provider rather than competing on price only.

## **Our Network**

We provide services using a complementary nationwide long-haul fiber-optic network with a hybrid wireline and fixed wireless local access network designed to optimize capital expenditures through the deployment of network access equipment based on specific customer requirements. Our last-mile access options include fixed wireless access technologies like proximity and symmetry, mobile or 802.16e WiMAX, point-to-point and point-to-multipoint wireless technologies, as well as metropolitan fiber rings. We switch our traffic using DMS equipment that interconnects with Telmex’s equipment and that of other local and long distance carriers in each city where we provide local service.

Our wireless network uses customer access equipment, microwave radios, DMS switching and other equipment supplied by various vendors, including Motorola, Airspan, SR Telecom, Nortel Networks and Siemens, among others. Our internet platform uses Cisco’s routing platform with Compaq servers and Microsoft



software applications. Our metropolitan fiber networks use Lucent Technology Allwave fiber and Nortel Networks DNX SDH equipment. The combination of these network components enables us to deliver world-class network reliability and service to our customers.

Through our current use of fixed wireless access technology, including Symmetry technology and WiMAX, we are able to provide our customers quality voice service and up to 8 Mbps data speeds. Currently, we provide voice and data packages to mass market customers with Internet speed access from 256 kbps up to 2 Mbps. We consider fixed wireless access technology to be ideal for our residential and micro and small business customers. Internet fixed wireless access technology, provides our customers with always-on data connections by using an internet protocol interface and dynamic timeslot assignments, which improves the data rates experienced by customers and also increases our network efficiency.

Basic voice and data services are delivered over all of our access technologies. Advanced data services and internet access with data rates ranging from 64 Kbps to 2,048 Kbps require deployment of additional equipment to support the customer's requirements. In general, the capabilities of the access technologies increase directly with the cost of the solution. Our hybrid access capability enables us to:

- provide a full range of voice, data and internet services;
- rapidly meet demand;
- penetrate specific target markets; and
- scale the infrastructure deployed to market demand and individual customer requirements.

This network infrastructure allows us to satisfy the requirements of diverse components of the market while maintaining a low-cost position relative to our competition.

#### *Build-out strategy*

Our local network has generally been built on a modular basis. Once a region of opportunity has been identified and the decision to expand has been made, we build our network in tandem with our sales efforts within the region. This approach provides greater flexibility and minimizes the time lag between the incurrence of capital expenditures and the generation of service revenues. This model differs significantly from a traditional wireline network covering the same geographic area in which the vast majority of capital expenditures are incurred prior to obtaining customer subscriptions.

#### *Last-mile connectivity*

The last-mile connectivity portion of our network is comprised of a mix of wireless technologies as well as fiber optics for customers within our metropolitan fiber optics rings. Our access technology is determined by cost-effectiveness analysis, customer applications and availability of service. We use fixed wireless access to serve customers requiring between one and nine lines of plain old telephony service ("POTS") in a single point of service. Point-to-multipoint is used for customers that require between 10 and 30 POTS and/or require low-speed (below 2,048 Kbps) dedicated private line accesses. Our point-to-point and fiber optics accesses are used for customers requiring digital trunks or dedicated private line accesses of more than 2Mbps. Hybrid solutions are being used in order to reach more customers by expanding service using digital loop concentrator and multi-tenant solutions.

We have contracts with Telefónica Data de Mexico, a subsidiary of Telefónica de España, pursuant to which we acquired the right to use capacity in Telefonica's long haul fiber infrastructure which is located between the northern border of Mexico and Mexico City. Pursuant to such contracts, Telefónica Data de Mexico has the right to use a pair of dark fibers in a portion of our metropolitan fiber rings. We also maintain a similar agreement with Telereunión to use approximately 620 kilometers of long distance fiber optic network in the Gulf of Mexico region.

### Local Network

As of December 31, 2009, our metropolitan fiber optic rings totaled 1,562 kilometers in the cities where we offer local services. Our local network is comprised of several technologies, including fixed wireless access, WiMAX, copper, point-to-point, point-to-multipoint and fiber optic links.

The following table summarizes our local infrastructure as of December 31, 2009.

City	Fixed Wireless Access Sites	Symmetry	Wimax	Point-to-Multipoint Sites(2)	Point-to-Point	Switches	Fiber (Kms)
Monterrey .....	64	19	63	30	390	8	372
Guadalajara .....	63	8	51	25	358	8	163
Mexico .....	159	34	112	68	1238	14	523
Puebla .....	20	5	23	9	120	1	70
Toluca .....	9	3	14	5	104	1	21
Leon .....	13	5	14	6	83	1	40
Queretaro .....	8	6	9	7	70	0	18
San Luis Potosi .....	11	5	15	5	31	0	24
Saltillo .....	7	5	10	4	52	0	37
Aguascalientes .....	9	5	11	5	30	0	15
Cd. Juarez .....	10	5	13	6	45	1	30
Tijuana .....	9	1	11	8	36	2	9
Torreon .....	7	5	12	4	55	1	18
Others .....	44	49	215	72	491	20	219
Total .....	433	155	573	254	3,103	57	1,562

### Long Distance Network

Our long distance fiber-optic network is approximately 7,700 kilometers in length using “non-zero dispersion shifted” fiber-optic, underground and optical-ground wire cable, which supports SDH and Dense Wavelength Division Multiplexing (“DWDM”) technology. SDH enables the deployment of bi-directional ring architecture, a system that allows for nearly instantaneous re-routing of traffic in the event of an equipment failure or a fiber-optic cut. DWDM technology enables expanded transmission capacity over the same physical infrastructure through the installation of additional electronics. Our long distance network connects 49 cities through owned infrastructure, and 154 additional cities through leased infrastructure as of December 31, 2009.

### Switching

We use 10 Nortel’s DMS-100 digital switches to route traffic in twenty two cities and 3 Nortel’s Call Server 2000 Softswitch to route traffic in ten additional cities. We have four Nortel DMS-250 digital switches for long distance services that are installed in the Main Switches Facilities to receive the traffic from close to 200 cities and international traffic from the U.S. and ROW. We have four Ericsson TL4 digital switches for local services, two located in Mexico, one in Monterrey and one in Guadalajara covering 16 cities. We use our A5020 Alcatel Softswitch used for Netvoice services and Internet Dialup. We have two SoftX3000 Huawei Softswitches that provide local services in eight cities and all the International VoIP traffic.

Our DMS-100 switches are capable of handling approximately up to 130,000 lines and the CS 2000 softswitches can handle up to 180,000, using the current software release. Both of these systems work on a modular basis and provide analog lines, E1 digital lines, digital high-speed data services, centrex services and operator assisted services. In addition, the CS2000 Softswitch can also provide multimedia capabilities by supporting multiple next generation protocols. Both switches can also provide private clear-channel digital lines, data transmission and value-added services such as four digit dialing, conference, call back, caller ID, call waiting, hot line and hunt group.

## Operational Support Systems

We have an information technology architecture that is based upon Siebel, a customer relationship management system, SAP software for enterprise resource planning, CSG Systems International software for billing and Net Boss, an advanced network management system. These systems enable us to perform on-line sales and service provisioning. We have been able to manage customer requests, generate accurate bills and produce timely financial statements. These systems allow us to respond to customer requests with speed, quality and accuracy.

We believe we have purchased sufficient spectrum to fulfill the capacity requirements of our business plan including the offering of broadband services to our customers. In September 1995, Avantel obtained a concession to offer local and long distance telephony services nationwide. In June 1996, Axtel also obtained a concession to offer local and long distance telephony services. Both concessions have a term of 30 years and, subject to the satisfaction of certain conditions, are renewable for an additional 30-year period.

We also hold concessions to use and exploit the following frequency bands:

- Two 929 MHz for radio messaging services;
- 50 MHz at 3.4 GHz, nationwide, divided into 9 regions for local telephony using fixed wireless access technology;
- 56 MHz at 7 GHz, nationwide, for long-haul point-to-point transport (a 50/50 ownership with Alestra);
- 60 MHz at 10.5 GHz, nationwide, for point-to-multipoint access;
- 60 MHz at 10.5 GHz in three regions for point-to-multipoint access;
- 168 MHz at 15 GHz, nationwide, for point-to-point access and transport;
- 368 MHz at 23 GHz, nationwide, for point-to-point access and transport; and
- 112 MHz at 37 to 38.6 GHz, in 5 regions, for point-to-point transport.

Each of the spectrum licenses has a term of 20 years and may be renewed at our option for additional 20-year periods as long as we are in compliance with all of our obligations thereunder and with any new conditions imposed in accordance with the law and as long as an agreement is reached on any new conditions set forth by the SCT. Our concessions are of a fixed duration and are scheduled to expire between 2018 and 2026.

The concession expressly permits us to provide the following services:

- basic local telephony;
- nationwide long distance telephony;
- the sale or lease of network capacity for the generation, transmission or reception of signs, signals, writings, images, voice, sounds or other information of any nature;
- the purchase and lease of network capacity from other carriers, including the lease of digital circuits;
- value-added services;
- operator services;
- data, video, audio and video conference services, except for cable or other restricted television, continuous music or digital audio services;
- credit or debit telephone cards; and
- public telephony services.

In November 2006, SCT granted, as part of Axtel's concession, a new permit to provide short message services ("SMS") to our clients. We have the required regulatory authority to provide such services to Mexico's entire population.

Some of our concessions require us to offer services in certain geographic areas where we are not currently offering services. With respect to those geographical areas in which we were required to provide such services by December 2008, we have complied with such coverage requirements. With respect to those geographical areas in which we are required to provide such services by December 2009 and our obligation to submit a social coverage program that must be previously negotiated with the SCT, we expect to comply with such requirements. However, if needed, we may request the necessary extensions from the SCT in order to comply with such coverage requirements. If we do not receive the necessary extensions when requested, the SCT could revoke the specific permits and concessions covering such territories in which we do not provide services. In the past we have been able to obtain extensions from the SCT in order to comply with such requirements and have been able to maintain in full force in effect our permits and concessions. Today, it is unlikely that SCT would revoke our concessions since we are currently offering services in most areas included in the existing nine telephone regions in Mexico. Specifically, we currently offer services in those areas where we were asked to provide service by SCT. The concessions for the geographic areas where we do presently offer our services cannot be adversely affected for these reasons.

### **Interconnection**

In accordance with the Federal Telecommunications Law, all holders of concessions for the installation, operation and exploitation of public telecommunications networks are required to provide interconnection services to other holders of public telecommunications network concessions.

All terms of interconnection (such as point of interconnection and interconnection fees) are negotiated between telecommunications concessionaires under COFETEL's supervision. Telecommunications concessionaires are prohibited from adopting discriminatory practices in the application of rates or any other terms of interconnection.

Agreements are typically signed for one-year periods. When agreements are renewed, parties can renegotiate new terms and conditions such as rates, technical aspects and minimum level of service conditions. If the parties do not come to an agreement, the previous existing conditions remain in place under an automatic extension until the parties reach a new agreement, maintaining the same rights and obligations until the new agreement is formalized. Parties can request that COFETEL intervene to resolve the conditions that cannot be agreed upon. By law, parties cannot cease to provide interconnection services to other carriers without a written authorization from SCT. In accordance with Mexican Telecommunications Regulations, we have established interconnection agreements depending on the type of traffic, as follows:

#### *Local interconnection*

Local interconnection agreements are established between two local fixed telephony providers in order to exchange local calls between their networks. Local interconnection agreements include provisions concerning local switched and non-switched interconnection, signaling, co-location and local transiting, among others.

The two most important conditions in local interconnection agreements are the per-minute interconnection fee and the "bill and keep" agreement. The current interconnection fee is US\$0.00975 per minute. We currently have two interconnection agreements with Telmex; one between Axtel and Telmex and another between Avantel and Telmex. The imbalance threshold under the bill and keep agreement refers to the difference between the outgoing and the incoming local traffic of any carrier. If at any given month, this difference falls below the permitted threshold, there are no payments among the carriers. If any carrier surpasses the threshold, payments have to be made between carriers for the full amount of the imbalance. The bill and keep agreements contain exceptions regarding internet traffic, long duration calls and traffic generated by call centers so that these exceptions will not affect the calculation of the permitted imbalance percentage.

*Axtel and Telmex's agreement.* Axtel entered into an interconnection agreement with Telmex in March of 1999. Axtel's interconnection agreement with Telmex expired on December 31, 2008. If the agreement expires without having been expressly extended by the parties, the agreement explicitly contemplates an automatic extension until both parties mutually agree to extend the expired agreement or execute a new interconnection agreement. The threshold for the differential between incoming and outgoing traffic set in this agreement is 5% and no payments have been made to Telmex since the implementation of this agreement.

*Avantel and Telmex agreement.* The Avantel interconnection agreement with Telmex was signed on October 1, 2006 and expired on December 31, 2008. The threshold for the differential between incoming and outgoing traffic set in this agreement is 5%. The agreement contains provisions for its continuous application; if it expires without having been extended by the parties, the agreement explicitly contemplates an automatic extension until both parties mutually agree to extend the expired agreement or execute a new interconnection agreement.

In addition to local interconnection agreements with Telmex, we have established interconnection agreements with most of the local fixed carriers, such as Teléfonos del Noroeste, S.A. de C.V. ("Telnor"), Alestra, Unefon and Maxcom, and some cable companies providing telephony services, representing more than twenty interconnection agreements in total. The terms and conditions for each agreement are similar to those established with Telmex.

#### *Mobile interconnection*

We have interconnection agreements with all cellular providers (including Telcel, Unefon, Iusacell and Telefónica Movil. As of December 31, 2008, the wireline to mobile interconnection fee under the calling party pays scheme payable to the cellular carriers was Ps. 0.603 per minute for Unefon, Iusacell and Telefónica Movil and Ps. 0.47 per minute for Telcel. In September 2008 and in response to an administrative procedure we initiated against Telcel, Telefonica, Iusacell and Unefon, the SCT determined fixed to mobile interconnection rates of Ps. 0.55 per minute payable to Telcel as of December 31, 2008, and Ps. 0.60 per minute payable to Telefonica, Iusacell and Unefon as of December 31, 2007. See "Business—Regulatory Proceedings."

#### *Long distance interconnection*

*Acting as local network.* These interconnection agreements allow long distance carriers to deliver long distance calls from their users to our local network. They also allow our users to make calls to non-geographic numbers (800s) assigned by COFETEL to such long distance carriers. We have long distance interconnection agreements in place with major long distance carriers such as LADA (Telmex and Telnor long distance operation) and Alestra, among others. Carriers that have not established this interconnection agreement with us, use traffic through LADA or other carrier that maintains an agreement with us. As of December 31, 2009, the interconnection fee we received from long distance carriers was either US\$0.0080 per minute or US\$0.0126 per minute (depending where the long distance call is delivered).

*Acting as long distance network.* These interconnection agreements which we have established with Telmex, Telnor and Maxcom, allow us to deliver long distance calls from our users to a local network. They also allow users of the local network to make calls to non-geographic numbers (800s) assigned by COFETEL to us. They also allow users of Telmex or Telnor who have chosen Avantel as their long distance carrier to use Avantel long distance services. As of December 31, 2009, the interconnection fee we pay to local carriers was either US\$0.0080 per minute or US\$0.0105 per minute (depending where the long distance call is delivered). Prices and tariffs charged under these long distance interconnection agreements are denominated in U.S. dollars and then converted into Mexican Pesos based on monthly exchange rates published by Banco de Mexico. See "Business—Regulatory Proceedings."

### *International settlement*

Mexican carriers entitled to operate an international gateway do not have any restriction on the volume of international traffic that they can terminate in Mexico, as long as they comply with the Mexican telecommunications regulations.

In addition, each carrier is free to negotiate the applicable rates for international calls terminating in Mexico. Prior to application, rates must be registered with COFETEL.

### **Customer Service**

A key element of our competitive strategy is to consistently provide reliable, responsive customer service. In order to achieve this goal, we have established a 24/7 customer service center for voice, data and internet services which is staffed by highly trained personnel. We have implemented a comprehensive training, testing and certification program for all staff that directly interacts with customers.

We provide post-sales service on a nationwide basis through the following:

- Customer Service provides post-sales customer support, ranging from general information, additions, moves and changes to billing inquires and technical support.
- Operator Service is 24/7, providing directory assistance, wake-up calls, time of day, emergency calls and placing domestic and international long distance calls.
- Repair Answer is our customer contact group that addresses and manages all customer trouble reports and provides on-line technical support and analysis.
- Local Test analyzes and tests all trouble reports that are not resolved on-line by Repair Answer. This team is accountable for routing “in service” and “out of service” trouble reports to Repair Dispatch. Both Repair and Local Test work closely with our network maintenance center in order to monitor and fix network disruptions.

Additionally, with the acquisition of Avantel we added two national management and monitoring centers located in Monterrey and Guadalajara.

### **Billing and Collection**

We believe our billing and collection process is an important aspect of our competitive advantage.

Our billing team receives and validates the call detail record from the network and bills customers on a monthly basis, typically within 14 days from the end of the billing period. Bills are due typically 25 days from the end of the billing period for mass market customers, while carriers, corporate and government customers have extended periods.

An ongoing revenue assurance process, which consists of reviewing the billing stream, payments and adjustments, as well as fraud detection and control, has become part of our regular billing operation. This process has contributed to minimizing fraud and risk.

To facilitate the reception of payments and to make the payment process convenient for customers, we have developed a number of payment reception channels. Some of these channels are:

- convenience stores;
- banks;
- Axtel MAPs (Axtel’s Sales and Payment Points);



- e-billing;
- Internet;
- supermarkets;
- automatic charges to credit cards, checking and debit accounts (upon customer approval); and
- TELECOM (Mexico's mail and telegraph company).

These channels provide easy and fast options for customers to select the most suitable and convenient alternative for a prompt payment.

To encourage customers to pay on time, we use preventive tactics such as calls to remind customers that have failed to pay promptly on their previous payment due dates and call interception. Additional procedures involve suspension of long distance and cellular outgoing calling, suspension of outbound calling and total suspension of service.

Past due accounts are turned over to external collections agencies 90 days after their due date (except for government accounts). Accounts are disconnected 180 days after their due date. Prior to disconnection, we conduct a negotiation of the outstanding balance with the customer as part of our retention efforts oriented to provide alternate solutions payment programs. Alternatives include reconnection of the service under a pre-payment scheme with a payment schedule for the outstanding balance.

## **Competition**

We compete primarily in the local telephony services market on the basis of features, customer service and value. Our direct competitors are wireline and fixed wireless local telephony operators. We also compete directly in the long distance market and we now provide long distance services separately from our local telephony service.

We believe there may be additional opportunities for consolidation in the Mexican telecommunications industry. Although it is not our main strategy, we intend to review and evaluate opportunities from time to time and, if an appropriate opportunity arises, we may pursue it through the strategic acquisition of assets or an acquisition of, or combination with, another company.

*Telmex.* Our main local telephony competitor is Telmex, the former state-owned telecommunications monopoly. Telmex has significantly greater financial and other resources than we have and serves all of the cities and markets that we serve. In addition, Telmex has an established customer base which represents the vast majority of the wireline local telephony lines in Mexico.

Telmex is the dominant provider of local telephony services and, as such, a significant number of our customers maintain an ongoing relationship with Telmex. Telmex has a presence throughout Mexico and its established and long-standing customer base gives it a substantial competitive advantage. See “Risk Factors—Risks Relating to Our Company—We depend on Telmex for interconnection and we may be forced to pay higher interconnection fees in the future, which could have a material adverse effect on our business and results of operations.”

With the convergence legislation enacted in 2006, Telmex will be able to provide video subject to obtaining the modification of its concession and complying with certain other obligations. Telmex's significant customer base provides significant leverage to develop the triple play services (voice, Internet and video) demand significantly. Telmex has publicly stated its intentions to offer triple-play services in the near future.



*Alestra.* Alestra commenced operations in 1996, providing only long distance telephony services to residential and business customers. In 2000, Alestra also started to offer local services to corporate customers in Mexico, Monterrey and Guadalajara, primarily. According to their 2008 20-F Report, Alestra is owned 49% by AT&T Telecom Mexico, Inc., a wholly owned subsidiary of AT&T Inc. and 51% by Onexa, S.A. de C.V., a corporation owned by Alfa, S.A.B. de C.V. Their network consists of 5,017 kilometers of long distance fiber and 1,084 kilometers of metropolitan rings. Due to the acquisition by the former SBC Communications Inc. of the former AT&T Corp., AT&T Inc. acquired certain obligations and restrictions with Alestra concerning direct competition and mandatory net margin contribution, among others, due to the significant ownership that the former SBC Communications Inc., now AT&T Inc., maintain in Telmex.

*Maxcom.* Maxcom commenced operations in 1999 targeting, initially, residential and small business customers in the cities of Puebla, Mexico City, Querétaro, San Luis and Tehuacan. More recently, through joint-venture agreements with other companies, they have added a small presence in the cities of Guadalajara, Monterrey and Toluca. Maxcom has deployed a wireline network in these cities and after nine years of operations, its customer base has grown to approximately 474,534 “revenue generating units” as of December 31, 2008.

*Cable Companies.* By virtue of the convergence legislation issued by COFETEL in October 2006, the largest cable companies in Mexico are now providing local telephone services to residential and small business customers in Mexico’s major cities, including many where we have operations. It is unclear what impact the recent alliance between Televisa and Nextel de Mexico will have on our business. However, assuming the related investment is consummated, Televisa’s cable companies, upon agreement with their minority shareholders, could add Nextel mobile services into their existing offers, making these bundled offers more appealing to customers. Further, we believe that the recent strategic partnership entered into between Nextel and Televisa will not have a material adverse effect on our operation and financial performance because our service agreement with Nextel will continue to be effective until its expiration date, regardless of the consummation of the Nextel-Televisa alliance.

*Other.* The legislative initiatives passed in 2006 created a legal framework for broadcasting companies to eventually provide voice and data services.

## Properties

All of our properties are located in Mexico. Our most important asset is our network infrastructure. See Note 6 in our audited consolidated financial statements.

Our corporate headquarters are located in Monterrey, Mexico. Our Monterrey office consists of 39,779 square meters. The lease on this property expires in 2015. We also own or lease office space and warehouses throughout the 39 cities where we operate. These are the facilities in which we have installed our switches and administrative offices. Office space or warehouses with more than 5,000 square meters include the following:

<u>Name</u>	<u>Use</u>	<u>Location</u>	<u>Area in m<sup>2</sup></u>	<u>Property</u>	<u>Contract Ending Date</u>
Headquarters Monterrey . . . . .	Administrative	Monterrey	39,779	Lease	25/05/2015
Voice Center Apodaca . . . . .	Operating Center	Monterrey	13,345	Lease	14/09/2005(1)
Call Center . . . . .	Operating Center	Santa Catarina	10,389	Lease	31/07/2011
Torre Axtel Santa Fe . . . . .	Administrative	Mexico	10,259	Lease	01/01/2011
Workcenter Alse Blanco . . . . .	Operating Center	Mexico	7,352	Lease	01/12/2011
Switch 1 . . . . .	Technology Facility	Guadalajara	5,550	Owned	—
CIC Apodaca . . . . .	Technology Facility	Monterrey	5,164	Lease	14/09/2005(1)
Cedis Santa Catarina . . . . .	Operating Center	Monterrey	5,012	Lease	20/07/2017

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- (1) The original term (ending date) set forth under the lease contract has expired. However, pursuant to applicable Mexican law and considering that there has been no opposition by the lessor with respect to the use of the property by the Company, the term of the lease contract has become undefined. The Company has a legitimate right to use the property until there is a termination notice by lessor as per applicable law. The terms and conditions of the original contract govern the relationship between lessor and the Company with respect to the property under use. If the Company were to receive a termination notice by lessor, the Company would have at least two months to return the property.

## **Employees**

As of December 31, 2009, we had 8,234 employees. All of our employees, except for our executive officers and certain other managers, are members of 2 different labor unions. We believe we have good relationships with our employees and their respective unions.

## **Legal Proceedings**

We are currently party to the following material legal proceedings:

### *Spectrasite Dispute*

In March 2002, Spectrasite Communications Mexico, S. de R.L. de C.V. (“Spectrasite Mexico”) filed an action against us in the 30th Civil Court in Mexico City. Spectrasite Mexico was seeking recovery of a deposit in the amount of US\$13.0 million that Spectrasite Mexico made with us in connection with a proposed sale-leaseback of towers. We, in turn, filed a counterclaim against Spectrasite Mexico and Spectrasite Communications Inc. for breach of contract in a related action. On December 15, 2004, Spectrasite Communications Inc. was duly served. On April 1, 2008, the trial court ruled against us ordering Axtel to return the deposit and applicable interests. The Company appealed the trial court’s decision before the Superior Court of Appeal. On March 2009, the Superior Court of Appeal ruled in our favor discharging us of our obligation to return the deposit and its interest and ordering Spectrasite Mexico to pay damages (*daños*) to us. Spectrasite Mexico and Spectrasite Communications Inc. have filed a constitutional review (*amparo*) challenging such State Superior Court’s decision; the resolution by the Federal Court is pending. See Note 21(c) to our unaudited consolidated financial statements for December 31, 2009 contained in this offering circular.

## **Regulatory Proceedings**

### *Axtel’s National Calling Party Pays Dispute*

In April 2006, COFETEL issued new general rules for the obligation to implement, on a national level, a “Calling Party Pays” model. Under this legal structure, the interconnection fees for national and international long distance calls were to be increased, which Axtel challenged in the administrative and judicial courts of Mexico. These proceedings have not yet been resolved, and we cannot determine with reasonable certainty the impact these proceedings would have if they are not resolved in our favor.

### *Avantel’s National Calling Party Pays Dispute*

In April 2009, COFETEL resolved the interconnection disputes initiated by Avantel against Telcel, Telefónica Movil, Iusacell and Unefon with respect to the interconnection fees arising from the termination of long distance calls under the National “Calling Party Pays” model. COFETEL’s decision established the same interconnection fees that were previously applied. The new resolutions were challenged by Avantel and by other mobile operators as well. We cannot determine with reasonable certainty the impact these proceedings may have if they are not resolved in Avantel’s favor.

### *Avantel's Local Calling Party Pays Dispute*

In August 2006, COFETEL resolved the interconnection disputes between Telcel and Avantel. In this resolution COFETEL approved a reduction of the interconnection fees to be paid by Avantel for calls terminated in Telcel's network for the years 2005 to 2010. Telcel challenged this resolution. These proceedings have not yet been definitively resolved, and we cannot determine with reasonable certainty the impact that these proceedings may have if they are not resolved in Avantel's favor.

### *Axtel's Local Calling Party Pays Dispute*

In August 2006, COFETEL resolved the interconnection disputes between Telcel and Axtel. In this resolution COFETEL approved a reduction of the interconnection fees to be paid by us for calls terminated in Telcel's network for the years 2005 to 2010. Telcel challenged this resolution. This proceeding was resolved confirming the reduced interconnection tariffs for the years 2005 to 2007. The new resolution has been challenged by us and also by Telcel, and we cannot determine with reasonable certainty the impact that these proceedings may have if they are not resolved in our favor.

During years 2007 and 2008, the Company started four administrative disputes concerning interconnection disagreements against Telcel, Iusacell, Telefónica Movil and Unefon in order to obtain new interconnection fees. On September 1, 2008, the SCT resolved these disputes. The decision issued by the SCT contemplated the application of new interconnection rates for years 2008 to 2011 for Telcel and for years 2006 to 2007 with respect to the other cellular telephone companies (Iusacell, Telefónica Movil and Unefon). Moreover, under the SCT decision, beginning from September 2008, the cellular telephone companies were obligated to bill the Company based on the real duration of the call. In addition, there is a possibility that the Company could assert claims for amounts that it paid in excess of the new rates during the period prior to September 1, 2008.

As a result of the decision issued by the SCT, the Company applied the new interconnection fees with respect to August 2008 traffic and onwards. Prior to the SCT's decision, Axtel and Avantel were paying Ps. 1.32 for each real minute to Telcel and Ps. 1.21 for each rounded minute to Iusacell, Telefónica Movil and Unefon. The new interconnection fees paid to by the Company to Telcel were Ps. 0.5465 per minute in 2008 and Ps. 0.506 per minute in 2009, and will be Ps. 0.470 per minute in 2010, and for years 2008 to 2010, the Company paid and will pay Ps. 0.6032 per minute to the rest of the cellular telephone companies. Avantel also adopted the rates mentioned above based on non-discriminatory treatment principles.

Nevertheless, all cellular telephone companies continued invoicing the Company for traffic termination under the "Calling Party Pays" model, applying the interconnection fees applicable prior to the SCT's decision. As of December 31, 2009, the difference between the amounts paid by the Company according to the new rates and the amounts invoiced by the cellular telephone companies amounted to approximately Ps. 950 million. See "Risk Factors—Risk Relating to Our Company—The Federal Tax and Administrative Court may rescind or nullify COFETEL's resolution approving a reduction in tariffs for termination of national long distance calls from Axtel to Telmex, which could have a material adverse effect on our business and results of operations."

Telcel and the other cellular telephone companies have challenged before the Federal Courts the decision issued by the SCT. As a consequence of these proceedings, Axtel and Avantel have a contingency reflected in their financial statements in the event that Federal Courts rule against the SCT decision and establish different rates than the ones determined by the SCT. The contingency reflected is to be calculated based on the difference between the rate established by SCT decision and the rates currently invoiced by the mobile operators.

With respect to the aforementioned SCT decision, the Company has knowledge that Telcel, Iusacell, Telefónica Movil and Unefon have asked the courts for a stay against the application of this new SCT decision and therefore are requesting to apply the rates prior to this decision until final resolution. The Company has only been served with respect to Telefonica's motion, and has not yet been served with respect to the other motions. These proceedings have not been resolved and we cannot determine with reasonable certainty the impact that these proceedings may have if the same are not resolved in our favor.

### *Interconnection Dispute Between Axtel and Telmex*

In March 2009, COFETEL resolved an interconnection dispute between the Company and Telmex with respect to the fees applicable for termination of national long distance calls from the Company to Telmex with respect to 2009. In this decision COFETEL approved a reduction in the interconnection fees charged by Telmex for terminating national long distance calls in their network with respect to those cities where Telmex does not have interconnection access points. These fees were reduced from Ps. 0.75 (US\$0.0574 calculated with the December 31, 2009 exchange rate of Ps. 13.0587 per U.S. dollar) per minute to US\$0.0105 or US\$0.0080 per minute (depending on the place where the interconnection is made).

Nevertheless, Telmex continues to invoice the Company for the termination of long distance calls at rates which applied prior to COFETEL's decision. As of December 31, 2009, the difference between the amounts paid by us according to the new rates and the amounts invoiced by Telmex is approximately Ps. 64.9 million before Value Added Tax, for which the Company has not established any reserves.

Telmex filed a complaint before the Federal Tax and Administrative Court (*Tribunal Fiscal y de Justicia Administrativa*) requesting the annulment of the COFETEL decision. Currently, this proceeding is in the discovery stage and resolution is pending.

Effective January 26, 2010, the Federal Tax and Administrative Court granted an injunction of the interconnection rates established by COFETEL. However, this injunction ceased to be effective on February 11, 2010, after the Company posted a surety bond granting an indemnity to Telmex, in the event that Telmex obtains a favorable judgment (i.e. the annulment of the new interconnection fees under COFETEL's decision), provided that such surety bond only covers lost interest on any unpaid amounts by the Company to Telmex.

We believe that the Federal Tax and Administrative Court will rule in our favor by confirming the decision issued by COFETEL; we have therefore recognized costs based on the fees approved by COFETEL. However, we cannot assure that the Federal Court will rule in our favor, in which case, COFETEL's decision may be declared null and void, having as a possible result an increase to the rates that the Company will have to pay Telmex with respect to the year 2009, and also, a possible retroactive application of the pre-existing Ps. 0.75 tariff, thereby compelling us to pay any unpaid amounts invoiced by Telmex during 2009.

With respect to the interconnection fees arising from the termination of national long distance calls payable by the Company to Telmex in 2010, an interconnection dispute between the Company and Telmex is still pending before the COFETEL. We believe that COFETEL will resolve in our favor by allocating a an interconnection fee consistent with its decision with respect to year 2009, in which case, this decision may also be challenged by Telmex.

### *Interconnection Dispute Between Avantel and Telmex*

The Avantel Interconnection agreement with Telmex provides for a non-discriminatory and most favorable customer treatment to Avantel, pursuant to which, along with non-discriminatory principles set forth under applicable law, Avantel applied the same fees determined payable by Axtel pursuant to the COFETEL resolution issued in March 2009 to the services provided to Avantel by Telmex.

Nevertheless, Telmex continues to invoice Avantel for the termination of long distance calls at rates which applied prior to COFETEL's decision mentioned above. As of December 31, 2009, the difference between the amounts paid by Avantel according to the new rates and the amounts invoiced by Telmex is approximately Ps. 699.5 million before Value Added Tax, for which there is no reserve. See "Risk Factors—Risk Relating to Our Company—The Federal Tax and Administrative Court may rescind or nullify COFETEL's resolution approving a reduction in tariffs for termination of national long distance calls from Axtel to Telmex, which could have a material adverse effect on our business and results of operations."

In February 2010, COFETEL resolved an interconnection dispute between Avantel and Telmex with respect to the applicable fees for the termination of long distance calls from Avantel to Telmex with respect to the year ended December 31, 2009. Pursuant to this decision, COFETEL approved a reduction in the rates for termination

of long distance calls applicable to those cities where Telmex does not have interconnection access points. These rates were reduced from Ps. 0.75 (US\$0.0574 calculated with the December 31, 2009 exchange rate of Ps. 13.0587 per U.S. dollar) per minute to US\$0.0126, US\$0.0105 or US\$0.0080 per minute, depending on the place where the interconnection is made.

Based on reduced rates approved in this decision, Avantel paid Telmex approximately Ps. 20.0 million in excess of what Avantel should have paid if the reduced rates authorized by COFETEL would had been applied effective during 2009. Management believes that Telmex will probably challenge this decision. We and our legal advisors are evaluating the steps to be followed.

As of December 31, 2009, Avantel and Axtel maintained a letter of credit for US\$34.0 million issued by Banamex in favor of Telmex to guarantee our obligations under several interconnection agreements. This letter of credit was delivered pursuant to certain interconnection and leasing capacity agreements among Avantel, Axtel and Telmex and is unrelated to the legal proceeding initiated by Telmex before the Federal Tax and Administrative Court. The full amount under the letter of credit was drawn by Telmex in January 2010, based upon its allegation of underpayments from Avantel. We believe that this drawdown was improper. Due to the fact that this situation is recent, we and our legal advisors are evaluating the steps to be followed.

#### *Other Regulatory Disputes*

In December 2005, COFETEL determined the proportion of call attempts that each of the operators with an international port had the right to collect from 1999 through 2004. Avantel challenged this resolution by initiating various administrative procedures. These proceedings have not yet been resolved, and we cannot determine with reasonable certainty the impact these proceedings would have if they are not resolved in our favor.

#### **Environmental, Health and Safety Matters**

We are subject to laws and regulations relating to the protection of the environment and human health and safety, including those governing the management and disposal of hazardous substances and wastes and the cleanup of contamination. As an owner or operator of property and in connection with the current or historical use of hazardous substances at our sites, we could incur costs, including cleanup costs, fines and third-party claims, as a result of violations of or liabilities under environmental or health and safety laws and regulations. We believe, however, that our operations are in substantial compliance with all such laws and regulations.

#### **Enforceability of Civil Liabilities Against Foreign Persons**

We and our subsidiaries (except for one subsidiary organized in the United States) are either public variable capital corporation, variable capital corporations, limited liability companies or fixed capital corporations organized under the laws of Mexico, and are headquartered, managed and operated outside of the United States (principally in Mexico). Most of our directors and officers reside in Mexico. All or a substantial portion of our assets and the assets of most of our directors and officers are located outside of the United States (principally in Mexico). As a result, it may not be possible for investors or our shareholders to effect service of process outside of Mexico or within the United States upon us or such persons, or to enforce a judgment obtained in the United States against us or them outside of Mexico or in the United States courts that is based on the civil liability provisions under laws of jurisdictions other than Mexico including the federal and state securities laws or other laws of the United States.

We have been advised by our special Mexican counsel, D&A Morales y Asociados, S.C., that no treaty is in effect between the United States and Mexico calling for the mutual recognition and enforcement of their respective judgments. The recognition by Mexican courts of a judgment rendered in the United States is usually done under the principle of reciprocity, which means that Mexican courts would reexamine judgments rendered in the United States if such foreign country would reexamine Mexican judgments. Mexican courts may enforce judgments rendered in the United States through a homologation procedure consisting of the review by such Mexican courts of the foreign judgment to ascertain whether certain requirements of due process, reciprocity and

public policy have been complied with, without reviewing the merits of the subject matter of the case; *provided* that all federal and state procedural requirements under Mexican law (as the applicable case may be), including laws concerning statute of limitations and expirations, are satisfied; and further *provided* that, among others:

- (1) such judgment is final in the rendering state and obtained in compliance with legal requirements of the jurisdiction of the court rendering such judgment and such judgment is in compliance with the terms set forth in the new notes and all legal requirements as the case may be;
- (2) such judgment is strictly for the payment of a certain sum of money, based on an *in personam* action (*acción personal*) as opposed to an *in rem* action (*acción real*);
- (3) the judge or court rendering the judgment is considered to have jurisdiction and is competent to hear and judge on the subject matter of the case in accordance with accepted principals of international law that are compatible and analogous with Mexican laws, and the subject matter of the case was not of the exclusive jurisdiction of Mexican courts;
- (4) service of process in the action has been served personally on the defendant or on a duly appointed process agent;
- (5) such judgment does not contravene Mexican law, public policy of Mexico, international treaties or agreements binding upon Mexico or generally accepted principles of international law;
- (6) the applicable procedure under the laws of México with respect to the enforcement of foreign judgments (including issuance of a *rogatory letter (carta rogatoria)* by the competent authority of such jurisdiction requesting enforcement of such judgment and the certification of such judgment as authentic by the corresponding authorities of such jurisdiction in accordance with the laws thereof) is complied with;
- (7) the courts of such jurisdiction would enforce Mexican judgments as a matter of reciprocity;
- (8) the action in respect of which such judgment is rendered is not the subject matter of a lawsuit or legal proceedings among the same parties that is or are pending before a Mexican court, or was resolved by or conflicts with a definitive judgment previously rendered by a Mexican court that has previously served process or delivered a rogatory letter (*carta rogatoria*) to the competent authorities in accordance with the Mexican law;
- (9) the court that rendered such judgment has jurisdiction over the debtor as recognized by the courts of Mexico and in accordance with its conflict of laws rules; and
- (10) the judgment fulfills all necessary requirements to be considered authentic.

Furthermore, there is doubt as to the enforceability, in actions originated in Mexico, of liabilities based in whole or in part on the United States federal or state securities laws, and as to the enforceability of judgments obtained in the United States in actions based in whole or in part on the civil liability provisions of United States federal or state securities laws.



## MANAGEMENT

Pursuant to our bylaws (*estatutos*) and Mexican law, management is entrusted to a Board of Directors and a Chief Executive Officer. The Board of Directors is composed of a maximum of 21 regular members and their respective alternate directors, as approved by a shareholders meeting. At least 25% of the members of the Board of Directors must be independent pursuant to Mexican Securities Market Law. Our Board of Directors currently is comprised of ten regular members and ten alternate directors. Pursuant to our bylaws and Mexican law, the members of the Board of Directors remain in office for thirty days after their resignation or conclusion of the term to which they were appointed unless replaced; the Board of Directors may appoint provisional members.

The following table presents information concerning our directors and executive officers as of December 31, 2009:

Officer	Age	Position
Tomás Milmo Santos.....	44	Chairman, Director and Chief Executive Officer
Felipe Canales Tijerina .....	51	Chief Financial Officer
Andrés Velázquez Romero(1) .....	44	Executive Director—Mass Markets and Alternate Director
Eduardo Alberto Morali Baz .....	57	Executive Director—Business Markets
Bruno Gustavo Ramos Maza .....	51	Executive Director—Strategic Accounts
Ivan Alonso Hernández.....	45	Executive Director—Technology and Innovation
Noe Garza Gonzalez .....	45	Executive Director—Network Operations
Alberto de Villasante Herbert(1).....	52	Executive Director—Negotiations, Alliances and Institutional Relations and Alternate Director
José Eloy Valerio Treviño .....	49	Executive Director—Human Resources and Processes
Gerardo González Villarreal.....	42	Audit Director
Thomas Milmo Zambrano .....	73	Director
Patricio Jiménez Barrera.....	43	Director
Alberto Santos de Hoyos.....	67	Director
Lorenzo H. Zambrano Treviño .....	65	Director
Alberto Garza Santos.....	45	Director
Héctor Medina Aguiar.....	58	Director
Bernardo Guerra Treviño(2)(3).....	44	Director
Fernando Quiroz Robles(2)(3).....	53	Director
Lawrence H. Guffey(2)(3) .....	41	Director
Balbina Milmo Santos(1) .....	38	Alternate Director
Francisco Javier Garza Zambrano(1) .....	54	Alternate Director
Alberto Santos Boesch(1).....	38	Alternate Director
David Garza Santos(1) .....	47	Alternate Director
Ramiro Villarreal Morales(1).....	61	Alternate Director
Mauricio Morales Sada(1) .....	47	Alternate Director
José Jorge Yañez Cervantes(1) .....	54	Alternate Director
Benjamin Jenkins(1) .....	39	Alternate Director

(1) The role of alternate director is to perform the role of the primary director if the primary director is not in attendance.

(2) Independent Directors.

(3) Member of audit and corporate practices committee.



Set forth below is a summary of the business experience, functions, areas of expertise and principal outside business interests of our current directors, alternate directors and senior management. The business address for each of our current directors, alternate directors and senior management is Blvd. Gustavo Díaz Ordaz km. 3.33 No. L-1, Col. Unidad San Pedro, San Pedro Garza García, N.L., Mexico, CP 66215.

**Tomás Milmo Santos** has held the position of Chief Executive Officer of Axtel since 1994 and Director since October 1997. Mr. Milmo was also appointed Chairman of the Board of Directors in October 2003. Prior to joining Axtel, Mr. Milmo worked at Carbonifera de San Patricio, S.A. de C.V., a mining company in Mexico. In 1988 he was named CEO of that same company, holding this post until 1990, when he founded and became CEO of Milmar, S.A. de C.V., a housing development company that developed and sold over 10,000 homes between 1990 and 1993. He is a member of the Board of Directors of Cemex, S.A.B. de C.V., HSBC Mexico S.A., Instituto Tecnológico de Estudios Superiores de Monterrey, A.C., Universidad de Monterrey, Promotora Ambiental, Instituto Nuevo Amanecer and NCCEP (the National Council for Community and Education Partnerships). Mr. Milmo holds a degree in Business Economics from Stanford University.

**Felipe Canales Tijerina** is Chief Financial Officer of Axtel since February 2009. Prior to joining Axtel, Mr. Canales spent 30 years at Alfa where he held several positions. Between 2007 and 2009 he held the position of Chief Financial Officer of Sigma Alimentos, a processed food company. Mr. Felipe Canales also served as a Director at Alestra, the telecommunications company jointly owned by Alfa and AT&T. Before his position in Sigma Alimentos, Mr. Canales was Senior Vice-President of Corporate Planning and Economic Studies, and Corporate Treasurer from 1996 to 2004. Mr. Canales has a Bachelor's Degree in Industrial Engineering from the Instituto Tecnológico y de Estudios Superiores de Monterrey and a MBA from The Wharton School at the University of Pennsylvania. Mr. Canales participated in the formation of Alestra.

**Andrés Velázquez Romero** has held the position of Executive Director of Mass Markets in Axtel since June 2009. Prior to his current position, Mr. Velazquez was Executive Director of Mass and Business Markets from March 2007 until May 2009. Mr. Velazquez has held various Senior Management positions in Axtel including Executive Director for Central Region and Treasurer and Administrative Director. Mr. Velázquez has been responsible for treasury, risk management, credit lines, funding structure and foreign exchange for a number of banking institutions. Prior to joining Axtel, he was the COO in charge of the Banca Serfín International Agency in New York. Mr. Velázquez holds a degree in Economics from the ITAM in México City.

**Eduardo Morali Baz** joined Axtel as Enterprise Market Executive Director in August 2009. Prior to joining Axtel, Mr. Morali worked at Cisco Mexico as Country Manager and before that he spent almost 9 years as Vice-President of the Enterprise Business Unit at Alestra. Before Alestra, Mr. Morali spent 5 years as President & General Manager for NCR Mexico including two years as Computer Division Vice-president for Latin America. Previously Mr. Morali worked for 21 years in IBM Mexico, holding several positions in Administration, Finance, Marketing and Sales. Mr. Morali has a Bachelor's degree in Business Administration from La Salle University and a degree in Finance from Instituto Tecnológico Autonomo de Mexico.

**Bruno Ramos Maza** has held the position of Strategic Accounts Executive Director since December 2006. Before the acquisition of Avantel by Axtel, he served as Avantel's Executive Director of Strategic Planning, Public Relations, International Traffic, Regulation and Legal affairs. Prior to that, Mr. Ramos directed efforts related to Strategic Planning for Banamex. Mr. Ramos has accumulated over fifteen years of experience in the telecommunications sector within different government and private organizations. Bruno Ramos has a B.S. degree in Electronics and Communications Engineering from Universidad Nacional Autonoma de Mexico and a specialization in Satellite Technology from Hughes Aircraft.

**Ivan Alonso Hernández** has held the position of Executive Director of Technology and Innovation since July 2009. Previously, Mr. Alonso was Chief Technology Officer, including network operations responsibilities since May 2002. Before then, Mr. Alonso held the Information Technology and Business Process Director positions at Axtel. Mr. Alonso has over 17 years experience in information technology and telecommunications areas with various companies, including Copamex Services & Real Estate Division. He has also collaborated

with financing institutions including Banco del Atlantico & Banpais, with responsibility for the telecommunications group of its Northeast Division. Mr. Alonso holds a B.S. degree in Electronics and Communications Engineering from the Instituto Tecnológico y de Estudios Superiores de Monterrey.

**José Eloy Valerio Treviño** has held the position of Executive Director of Human Resources and Processes since June 2007. Prior to his present position, Mr. Valerio was Director for Planning of Human Resources & Human Development at Axtel. Mr. Valerio has 26 years of experience in Human Resources and Administration in which he has carried out directive and consultant positions at Telecommunications, Paper and Cellulose, Tourism, Steel-Mechanical, Automotive and Pharmaceutical Industry. He was President of the Human Resources Executives Association (“ERIAC”) and has been an Advisor for Academic, Governmental and Non-Governmental Organizations. Mr. Valerio holds a degree in Administration and an M.B.A.

**Gerardo Gonzalez Villarreal** has held the position of Audit Director in Axtel since March 2000. Prior to his current position, Mr. González held the Comptroller Director position. Mr. González has over 20 years experience in the audit, tax and accounting field. Prior to joining Axtel, he collaborated with international accounting firms such as Coopers & Lybrand International and DFK International, and was a member of the Mexican and International DFK Audit Committee, in his capacity as Chairman in the Mexican accounting firms. Mr. González holds a degree as CPA & BA from Universidad del Norte.

**Thomas Milmo Zambrano** has been a Director of Axtel since October 1997 and held the position of Chairman of the Board of Directors from October 1997 until 2003. Mr. Milmo Zambrano was founder and Chairman of Grupo Javer S.A. de C.V., one of the largest housing development companies in Mexico, and of Incasa, S.A. de C.V., one of the largest aggregate producers in Mexico. He was also Chairman and CEO of both Carbonifera de San Patricio S.A. de C.V. and Carbon Industrial, S.A. de C.V., medium-sized mining companies in Mexico. He was a Director of Cemex, S.A. de C.V. until 1996.

**Patricio Jiménez Barrera** has been a Director of Axtel since 1998 and held the position of Chief Financial Officer of Axtel from January 1998 until March 2009. Prior to joining Axtel, Mr. Jiménez held a variety of finance-related positions, including investment banker while at InverMexico Casa de Bolsa, a corporate treasurer while at Grupo Cydsa, S.A. and an investment banker, international treasurer, financing and correspondent banker while at Banca Serfín, S.A. (Mexico’s third largest bank). Immediately prior to joining Axtel, Mr. Jiménez was responsible for the International Division at Banca Serfín, S.A. He is a member of the board of Seguros Banorte Generali and Pensiones Banorte Generali. Mr. Jiménez is a CPA and holds a degree from the Instituto Tecnológico y de Estudios Superiores de Monterrey.

**Alberto Santos de Hoyos** Founding member and Member of the Board since 1997. He is a Member of the regional Board of Banco de Mexico, Board Member of Grupo Cydsa, Grupo Senda and Madisa. He has been a Senator and Representative in the Mexican Congress, President of the Nuevo León Chamber of Industry (CAINTRA), Vice President of the Confederation of Industrial Chambers (CONCAMIN) and President of the National Chamber of the Sugar and Alcohol Industries. He was Chairman of the Board, CEO and a Member of the Board of Gamesa. He is currently a Member of the Boards of Desarrollo Social, Casa Paterna La Gran Familia, Andares, Instituto Nuevo Amanecer, Renace, Admic and Patronato Pro Educación Marista, and Chairman of the Boards of Empresas Santos, Ingenio Santos and Tres Vidas. Mr. Santos holds a degree in Business Administration from Tecnológico y de Estudios Superiores de Monterrey.

**Lorenzo Zambrano Treviño** Founding member and Member of the Board since 1997. He is CEO and Chairman of the Board of Cemex, S.A.B. de C.V. and Chairman of the Board of Instituto Tecnológico de Estudios Superiores de Monterrey, A.C. He is a Member of the Board of IBM and a Member of the International Advisory Boards of Allianz and Citigroup. He is also a Member of the Boards of Alfa, Femsa, Grupo Financiero Banamex, and Televisa, as well as a Member of Stanford University’s Graduate School of Business Advisory

Council and of the Board of Monterrey's modern art museum, MARCO. Mr. Zambrano holds a B.S. degree in Mechanical Engineering from the Tecnológico de Monterrey and an M.B.A. from Stanford University.

**Alberto Garza Santos** has been a Director of Axtel since October 2003. Mr. Garza is the founder and Chairman of the Board of Promotora del Viento, S.A de C.V., a company dedicated to wind power in Mexico. He is also founder and Chairman of the Board of Promotora Ambiental, S.A.B. de C.V. (PASA), a leading waste management company in Mexico. Mr. Garza has engineered PASA's growth through multiple acquisitions, local unit start-ups, municipal concessions and the development of world-class landfills, including Mexico's first five privately owned landfills. In 2002, he positioned PASA as PEMEX's waste services provider of choice, winning various large, multiyear contracts.

**Héctor Medina Aguiar** has been a Director of Axtel since October 2003. Mr. Medina held the position of Executive Vice-President of Legal and Finance of Cemex, S.A.B. de C.V. until February 2010. Before joining Cemex, Mr. Medina was a Senior Manager at Grupo Alfa S.A. de C.V. He is Chairman of the Board of Universidad Regiomontana, Board Member of Minera Autlan, Cementos Chihuahua, Nacional Monte de Piedad and Mexfrutas. Mr. Medina is also member of the Advisory Committee of the Monterrey Institute of Technology (Instituto Tecnológico y de Estudios Superiores de Monterrey). Mr. Medina is a graduate of the Instituto Tecnológico y de Estudios Superior de Monterrey with a degree in Chemical Engineering. He also holds an M.S.C. degree in Management from the University of Bradford Management Center in England and an M.S. degree from the Escuela de Organización Industrial in Spain.

**Bernardo Guerra Treviño** has been a Director of Axtel since April 2006. Chief Executive Officer, and founding member in 1995, of MG Capital, an independent asset management firm in Mexico. From 1986 to 1995, he held different positions in financial institutions in Monterrey. Mr. Guerra holds an Industrial Engineering degree from the Instituto Tecnológico y de Estudios Superiores de Monterrey. He currently serves in the Board of Director of Promotora Ambiental S.A.B. de C.V.(PASA) and Banco Ahorro Famsa S.A.

**Fernando Quiroz Robles** Member of the Board of AXTEL since April 2007. He is Chairman of the Board of Acciones y Valores Banamex, S.A. de C.V., a brokerage house that is part of Grupo Financiero Banamex ("Accival"), and Head of Citigroup Latin America's Corporate and Investment Banking Division. At Citigroup, he is also a member of the Committee for Administration and Investment Banking and of the Planning Committee. He previously occupied several executive positions with Banamex and Citigroup in areas such as retail banking, international banking and strategic planning and economic analysis. He began his career with Banamex in 1979.

**Lawrence H. Guffey** Member of the Board since 2000 and a Member of the Audit and Corporate Practices Committees. He is Senior Managing Director of Blackstone Group International. He previously worked in the Acquisitions Group at Trammell Crow Ventures, the principal investment arm of Trammel Crow Company. He is a Member of the Boards of Cineworld Group PLC, Deutsche Telekom and TDC.

**Francisco Javier Garza Zambrano** has been an Alternate Director of Axtel for Mr. Lorenzo Zambrano Trevio since June 17, 2005. Mr. Garza holds the position of President of the America region. He has been Chairman of Cemex Mexico, Cemex Panama, Venezolana de Cementos (Vencemos, S.A.), Vice President of Trading Cemex, S.A. and Chairman in charge of Cemex, S.A. de C.V.'s operations in the United States. Mr. Garza holds a degree in Business Administration from the Instituto Tecnológico y de Estudios Superiores de Monterrey and an M.B.A. from Cornell University-Johnson Graduate School of Management.

**Alberto Santos Boesch** has been an Alternate Director of Axtel for Mr. Alberto Santos de Hoyos since June 17, 2005. Mr. Santos has held the position of Chief Executive Officer at Empresas Santos, S.A. since the year 2000. He is a shareholder and director of Grupo Tres Vidas Acapulco, S.A., Desarrollos Marinos del Caribe (Hotel Mandarin Oriental Rivera Maya) and Gimnasio Body-tek, S.A. Mr. Santos is also a member of Generación 2000 and Grupo Mexico Nuevo. He is currently the Chairman of the Board of Directors of Grupo Monde (Mundo de Adiverzas theme park). Mr. Santos holds a degree in International Studies from the Universidad de Monterrey as well as international studies from Cushing Academy.

**David Garza Santos** has been an Alternate Director of Axtel for Mr. Alberto Garza since November 2005. Mr. Garza is Chairman of the Board of Directors and Chief Executive Officer of Maquinaria Diesel, S.A de C.V., a company which distributes Caterpillar, Ingersoll Rand and other construction equipment in Mexico and is also Chairman of the Board of Directors of Comercial Essex, S.A. de C.V., which is the largest distributor of Exxon Mobil lubricants in Mexico. Mr. Garza is also a member of the Board of Directors of Desarrollos Delta, S.A. de C.V., a real estate developer for residential, offices and resorts in Mexico, a member of the Board of Directors of Promotora Ambiental, S.A. de C.V., a leading waste management company in Mexico and also a member of the Advisory Committee of the School of Business Administration of the Instituto Tecnológico y de Estudios Superiores de Monterrey. Mr. Garza holds a degree in Business Administration from the Instituto Tecnológico y de Estudios Superiores de Monterrey.

**Ramiro G. Villarreal Morales** has been an Alternate Director of Axtel for Mr. Héctor Medina Aguiar since April 2006. Mr. Villarreal is the General Counsel of Cemex S.A.B. de C.V. since 1987. Mr. Villarreal is also Secretary of the Board of Directors of Cemex S.A. de C.V. since 1995. Prior to joining Cemex, he served as Assistant General Director of Grupo Financiero Banpais (now part of Banco Mercantil del Norte S.A.) from 1985 to 1987. Mr. Villarreal is a graduate of the Universidad Autonoma de Nuevo Leon with a degree in law and holds a Master of Science in Finance from the University of Wisconsin.

**Mauricio Morales Sada** has been an Alternate Director of Axtel for Mr. Bernardo Guerra Treviño since April 2006. Mr. Morales Sada is president, and founding member in 1995, of MG Capital, an independent asset management firm in Mexico. From 1984 to 1995, he held different positions in financial institutions in Monterrey. Mr. Morales holds a Mechanical Engineering degree from the Instituto Tecnológico y de Estudios Superiores de Monterrey, and currently serves in the Advisory Committee for the Business Incubator of the same institute.

**Benjamin Jenkins** has been an Alternate Director of Axtel for Mr. Lawrence H. Guffey since October 2003. Mr. Jenkins is a Principal in the Private Equity group of Blackstone. Since joining Blackstone in 1999, Mr. Jenkins has been involved in the execution of Blackstone's investment in Axtel and has evaluated numerous industrial and communications investments. Previously, Mr. Jenkins was an Associate at Saunders Karp & Megrue. Prior to that, Mr. Jenkins worked in the Mergers & Acquisitions Department at Morgan Stanley & Co. Mr. Jenkins holds a B.A. in Economics from Stanford University and an M.B.A. from Harvard Business School.

**Alberto de Villasante Herbert** has held the position of Executive Director of Negotiations, Alliances and Institutional Relations and alternate director of Axtel since March, 2007. Previously, Mr. De Villasante was Vice-president of Negotiations, Alliances and Institutional Relations, responsible for relations with regulators, purchases of strategic assets, real estate, public telephony and Axtel's strategic alliances. Prior to joining Axtel, he occupied several positions in Xignux including CEO of Multilec. He is a member of the Board of Directos of Concreta S.A of C.V. and Productora de Terrasos S.A. de C.V. He holds a degree in Marketing from the Instituto Tecnológico de Estudios Superiores de Monterrey, A.C. and a Masters of public accountant, administration and total quality.

**José Jorge Yáñez Cervantes** has held the position of Head of Corporate Development for Banamex/Citigroup for Mexico and Latam since June 2007. Prior to his current position, Mr. Yáñez held various Senior management positions in Banamex, including Executive Vice-president of Strategy and Business Development. Mr. Yáñez has over 30 years experience in finance, investment banking, mergers and acquisitions and business development. He also has been member of the Board of Directors of various companies in which Banamex is a stockholder. Mr. Yáñez holds an Administration Masters Degree from the Instituto Tecnológico de Estudios Superiores de Monterrey, A.C.

**Noé Garza González** has held the position of Executive Director of Infrastructure Operations since July, 2009 and was previously Director of Network Administration Operations and Maintenance since October 2002. Mr. Garza has over 22 years of experience in the telecommunications industry. Prior to joining Axtel in December 1999, Mr. Garza was Director of Network Planning and Engineering for Iridium Central America and

México. He also collaborated for over 5 years with Celular de Telefonía (Cedotel) in the deployment and management of the first cellular telephony network in the northeast part of México. Mr. Garza has a Bachelor's degree in Systems Engineering, an MBA from the University Autonoma de Nuevo León and he also holds a degree in International Management from the University of Phoenix.

*Balbina Milmo Santos* was born on October 8, 1970 in Monterrey, N.L. She holds a degree in Graphic Design from the Instituto de Arte y Restauo de Florencia, Italia. She has also pursued studies at the Chamberlayne School of Design in Newton, MA. She has also conducted several activities as an entrepreneur.

Thomas Milmo Zambrano is the father of Tomas and Balbina Milmo Santos and cousin of Lorenzo Zambrano. Alberto Santos de Hoyos is the uncle of Tomas Milmo Santos, Alberto Garza Santos and David Garza Santos and the father of Alberto Santos Boesch.

For the year ended December 31, 2009, the aggregate compensation, including benefits, we paid to our directors, alternate directors and executive officers for services in all capacities was approximately Ps. 64.0 million.

### **Audit and Corporate Practices Committee**

The Board of Directors in its supervision activities, will be assisted by one or more committees. For corporate practice matters, a committee will: provide its opinion to the Board of Directors with respect items of its concern as set forth under Mexican Securities Market Law; request expert opinions when considered advisable; call for shareholders meetings; provide support to the Board of Directors on reports needed to be prepared; and all other actions provided for under Mexican Securities Market Law or set forth under the bylaws. For audit matters, the same committee will: provide its opinion to the Board of Directors with respect items of its concern as set forth under Mexican Securities Law; evaluate the audit firm's performance; discuss the financial statements for the company and recommend their approval to the Board of Directors; report the Board with the status of the internal control and audit systems of the company; render the opinion with respect the accounting policies and criteria and financial information submitted by the Chief Executive Officer; assist the Board of Directors by preparing the necessary reports; request expert opinions when considered advisable; request the relevant officers reports related with financial information as may be deemed necessary; investigate possible failures to comply with the policies and guidelines related to the operations, internal control systems and audit; receive information submitted by shareholders, directors, officers, employees or any third party with respect the items set forth on the items described in the previous item; inform the Board of Directors of any important irregularity detected in connection with the corrective actions proposed; call for shareholders meetings; verify that the Chief Executive Officer complies with resolutions adopted at the shareholders and board of directors meetings.

Our audit and corporate practices committee consists of Bernardo Guerra Treviño, Lawrence H. Guffey and Fernando Quiroz Robles and their respective alternates, Mauricio Morales Sada, Benjamin Jenkins and José Jorge Yañez Cervantes. Our shareholders meeting appointed Mr. Bernardo Guerra Treviño as Chairman of such committee.

### **Compensation Committee**

The shareholders' meeting of the Company approved the elimination of the compensation committee. Most of the duties and responsibilities of our former compensation committee have been assumed by our Board of Directors and our Audit and Corporate Practice Committee.

### **Risk Committee**

On April 24, 2009, the Board of Directors created a risk committee to oversee derivatives transactions in respect of notional amounts in excess of US\$30 million.



## PRINCIPAL SHAREHOLDERS

Mexican law limits foreign ownership of telecommunications companies which, like Axtel, own certain telecommunications concessions to 49% of the voting stock of such companies. Share ownership of directors, senior management and other beneficial owners of 5% or more of the Company's shares as of December 31, 2008, is as follows:

Name	Position	Series A	% of total ownership	Series B	CPOs(1)	% of total ownership	% total
Tomás Milmo Santos . . . . .	Chairman, CEO	27,855,354	0.3%	3	170,000,959	13.7%	13.9%
Thomas Milmo Zambrano . . . . .	Director	17,369,850	0.2%	12	97,909,183	7.9%	8.0%
Alberto Santos de Hoyos . . . . .	Director	15,505,689	0.2%	15	64,362,365	5.2%	5.3%
Credit Suisse & BBVA(2)(3) . . . . .	N.A.	—	—		119,000,000	9.6%	9.6%
Telecomunicaciones Holding Mx(3)(4) . . . . .	N.A.	—	—	—	n.a	Between 7% and 10%	Between 7% and 10%

- (1) One CPO is equal to seven Series B shares.
- (2) As foreign holders this entity must hold their Series B shares beneficially through CPO's or ADS's.
- (3) 50% Credit Suisse and 50% BBVA share ownership through 3-year forward agreement with Impra Café S.A. de C.V., a subsidiary of Cemex S.A.B. de C.V. Based upon information available to the Company as of March 31, 2008.
- (4) Based upon information available to the Company as of April 16, 2009.

The following directors and executives own less than 1% of the Company's shares as of December 31, 2008:

Patricio Jiménez Barrera . . . . .	Director
Alberto Garza Santos . . . . .	Director
Bernardo Guerra Treviño . . . . .	Director
Alberto de Villasante Herbert . . . . .	Alternate Director, Senior Management
Balbina Milmo Santos . . . . .	Alternate Director
Francisco Garza Zambrano . . . . .	Alternate Director
Alberto Santos Boesch . . . . .	Alternate Director
Andrés Velázquez Romero . . . . .	Alternate Director, Senior Management
David Garza Santos . . . . .	Alternate Director
Mauricio Morales Sada . . . . .	Alternate Director
Noe Garza Gonzalez . . . . .	Senior Management
Jose Eloy Valerio Treviño . . . . .	Senior Management
Gerardo Gonzalez Villarreal . . . . .	Senior Management

The remaining directors and senior executives do not own any Company shares as of December 31, 2009:

None of the shares held by Directors or Senior Management grant to their holders different voting rights.

As of December 31, 2009 (except as otherwise noted), there are no arrangements for involving employees in the capital of the Company or any arrangement that involves the issue or grant of options or shares or securities of the Company.

## CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

### **Merger Agreement**

On August 26, 2005, we and our former shareholder Telinor entered into a Merger Agreement providing for the Merger of Telinor with and into Axtel. The Merger was effective on September 13, 2005, after which Telinor ceased to exist and Axtel survived with its current corporate name. As a result of the Merger and pursuant to the terms of the Merger Agreement, the equity holders of Telinor are now shareholders of Axtel. The Merger was duly approved by an extraordinary shareholders' meeting of Axtel and by an extraordinary partners' meeting of Telinor.

### **Resolution of Shareholdings Dispute**

On August 26, 2005, we, Telinor, Blackstone Capital Partners III Merchant Banking Fund L.P., Blackstone Offshore Capital Partners III L.P. and Blackstone Family Investment Partnership III L.P. (collectively, "Blackstone"), LAIF X sprl and LAIF IV Ltd. entered into a settlement agreement (the "Settlement Agreement") pursuant to which all issues in an arbitration and other previously disclosed judicial proceedings in the United States and Mexico relating to the issuance and ownership of certain of our shares were resolved. As a consequence of the Settlement Agreement, our shareholders held an extraordinary shareholders meeting on August 26, 2005 pursuant to which, among other matters: they acknowledged and ratified all current shareholdings in Axtel including the issuance and subscription of the previously issued shares which were the subject of dispute; they authorized a decrease in an immaterial amount in Telinor's and Blackstone's ownership of our shares and an increase in the same amount in LAIF X sprl's ownership share, approved the Merger of Telinor and Axtel and a number of ancillary matters. All of the proceedings between the parties to the Settlement Agreement with respect to the matters previously in dispute have been definitely resolved.

### **Banamex and/or Citigroup Inc. Agreements**

#### *Banamex Working Capital Facility*

In January 15, 2010 Banamex granted Axtel a US\$32.0 million working capital loan that contains customary conditions and matures on July 15, 2010.

#### *Term Loan Facility*

On November 30, 2006 we entered into an unsecured credit agreement with Citibank, N.A. as the Administrative Agent and Banamex as the Peso Agent, which was subsequently amended and restated on February 23, 2007, with a peso tranche in the aggregate amount of Ps. 1,042.0 million and a U.S. dollar tranche in the aggregate amount of US\$110.2 million. In September 2009, we made a principal prepayment of the U.S. dollar tranche of US\$85.0 million. The term loan facility will mature in February 2012, with partial principal repayments payable quarterly starting in February 2010. The facility was syndicated with thirteen Mexican and international financial institutions. See "Description of Other Indebtedness."

#### *Banamex Master Services Agreement*

On November 27, 2006, Axtel, Avantel and Banamex entered into a master services agreement in which it was agreed that all service agreements in effect between Avantel and Banamex as of the date of the acquisition would survive with substantially identical terms and Axtel would provide telecommunications services (including, local, long distance and other services) to Banamex and its affiliates located in Mexico. During the term of the agreement, Banamex has agreed to contract with us for all of its current and future telecommunications needs, and we have agreed to grant Banamex a most favored customer benefit with respect to rates and services levels. The initial term of this agreement is for five years, with automatic renewal for similar periods of five years if at that time of renewal we are not in breach of our obligations.



### *Banamex Credit Agreement*

On December 7, 2006, Avantel Concesionaria and Banamex entered into a credit agreement under which Avantel Concesionaria issued a standby letter of credit in favor of Telmex and Telnor for an amount of US\$60.0 million to secure payment of services rendered by Telmex and Telnor in connection with the interconnection agreement dated as of October 1, 2006 among Telmex, Telnor and Avantel Concesionaria. The standby letter of credit amount was reduced to US\$34.0 million and its expiration date was extended to December 2010. On January 8, 2010, Telmex requested to draw on the letter of credit, which request was honored by Banamex and subsequently paid by the Company on January 13, 2010. There is no more availability under this standby letter of credit. In March 2009 we signed another letter of credit for US\$5.1 million between AXTEL and Banamex.

### *TelHolding Agreement*

On November 30, 2006, we entered into an agreement with Tel Holding whereby Tel Holding was granted the option to subscribe for a number of shares (in the form of CPOs) representing up to 10% of our outstanding shares. Pursuant to this subscription agreement, Tel Holding subscribed and paid for 82,151,321 Series B shares in the form of CPOs on January 4, 2007. According to the terms of this subscription agreement, Tel Holding agreed not to transfer any of the CPOs acquired pursuant to such subscription agreement for a period of 364 days following the date of the acquisition of such CPOs, except in certain circumstances. In addition, Tel Holding was granted the right to request us to assist and support them, at our expense, in preparing and issuing placement prospectus and in participating in investor meetings for the offer of the CPOs, *provided* that (i) three years have elapsed since the acquisition of the CPOs by Tel Holding and (ii) such offer is made in any securities exchange where the CPOs representing our shares are trading at the time.

### *Blackstone's Advisory Services*

We have engaged and may continue to engage The Blackstone Group and certain of its affiliates from time to time in connection with strategic advice related to our business.

### **Other Transactions**

In March and May 2000, we and Gemini, S.A. de C.V. (a company controlled by Alberto Garza Santos, one of our shareholders) entered into lease agreements for the lease of land and property on which our corporate offices and a switch are located. For the period beginning January 1, 2002 and through December 31, 2006, we paid Gemini approximately US\$10.6 million in rental payments under these leases. In 2007, the agreement was modified and signed between Axtel and Inversiones DD. For the period beginning January 1, 2007 and through December 31, 2009, we paid Inversiones DD approximately US\$4.5 million in rental payments under these leases.

In August 2002, we and Neoris de Mexico, S.A. de C.V. (a consulting firm indirectly controlled by an affiliate of Imprá Café, S.A. de C.V., one of our shareholders) entered into a professional services agreement for the provision of technical assistance to us with respect to a customer care platform. From January 1, 2008 through December 31, 2009 we paid an aggregate amount of US\$4.1 million in service fees.

In April 2002, we and Instalaciones y Desconexiones Especializadas, S.A. de C.V. (a company controlled by the son of Alberto Santos de Hoyos, one of our shareholders) entered into a services agreement for the provision of installation services with regard to customer premise equipment. For the period beginning April 1, 2002 and through December 31, 2009, we paid them approximately US\$5.8 million in fees for services.

We and Operadora de Parques y Servicios. S.A. de C.V. (a company controlled by the son of Alberto Santos de Hoyos, one of our shareholders) entered into a service agreement dated February 16, 2005, for the marketing and advertising of Axtel inside a theme park. For the period beginning January 1, 2002 and through December 31, 2009, we paid them approximately US\$1.3 million in related fees.

Fundación Axtel A.C., a non-profit charity, was founded in 2005 to promote provide assistance in the communities where we operate. Among others, Tomas Milmo Santos and Patricio Jimenez serve as Directors in Fundación Axtel. In each of the years ended December 31, 2008 and 2009, we contributed US\$1.0 million to Fundación Axtel.

On November 24, 2006, our shareholders Thomas Milmo Zambrano, Maria Luisa Santos de Hoyos, Alberto Santos de Hoyos, Tomas Milmo Santos and Imprá Café, S.A. de C.V., entered into a shareholders agreement whereby they agreed, among other things, to vote their shares (in any meeting of shareholders whereby the members of the board are to be elected) in order to designate one director (and its alternate) to our board as proposed jointly by Citigroup Inc., its subsidiaries and Tel Holding and its assigns, so long as such entities collectively hold or beneficial own (directly or indirectly through CPOs) shares representing between 7% and 10% of our outstanding shares.

## DESCRIPTION OF OTHER INDEBTEDNESS

The following is a description of our other indebtedness.

### **2012 Term Loan Facility**

On November 30, 2006 we entered into an unsecured credit agreement with Citibank, N.A. as the Administrative Agent and Banamex as the Peso Agent, which was amended and restated on February 23, 2007 (the “2012 Term Loan Facility”). The 2012 Term Loan Facility has a peso tranche in the aggregate amount of Ps. 1,042,362,416.67 and a U.S. dollar tranche in the aggregate amount of US\$110,225,133.28. The term loan facility will mature on February 2012, with partial principal repayments payable quarterly starting in February 2010. The following is a summary of certain terms of the term loan facility:

#### *Interest Rate and Fees*

The borrowings under the U.S. dollar tranche bear interest at a rate equal to an applicable margin plus, at our option, either (a) a base rate determined by reference to the higher of (1) the reference rate of the applicable agent and (2) 0.50% per annum above the latest federal funds rate or (b) a LIBOR rate determined by reference to the costs of funds for deposits in U.S. dollars for the interest period relevant to such borrowing divided by one minus the reserve requirement percentage specified by the Federal Reserve Board or other governmental authorities. The applicable margin for borrowings under the U.S. dollar tranche is 0.50% per annum with respect to base rate borrowings and 1.50% per annum with respect to LIBOR borrowings. The borrowings under the Peso tranche bear interest at a rate equal to TIIE (*Tasa de Interes Interbancaria de Equilibrio*) plus 1.50% per annum.

#### *Prepayments*

We may make voluntary prepayments on the outstanding loans at any time without premium or penalty, except for customary “breakage” costs with respect to LIBOR loans.

#### *Guarantee*

All obligations under the term loan facility are unconditionally guaranteed on a joint and several basis by each of our existing and future direct and indirect subsidiaries, subject to certain exceptions for immaterial subsidiaries, referred to collectively as the Guarantors.

#### *Certain Covenants*

Our term loan contains a number of covenants that, among other things, restrict, subject to certain exceptions, our ability and our restricted subsidiaries ability to:

- sell assets;
- engage in mergers and acquisitions;
- pay dividends and distributions or repurchase our capital stock;
- incur additional indebtedness (including guarantees and other contingent obligations);
- make investments and loans;
- create liens on assets;
- engage in certain transactions with affiliates;
- change our business or ownership;
- make prepayments relating to other indebtedness;

- amend or waive provisions of charter documents in a manner materially adverse to the lenders; and
- change our fiscal year or accounting policies.

In addition, the term loan facility requires us and our subsidiaries to maintain the following financial covenants:

- a minimum net worth of 80% of our net worth upon consummation of the acquisition;
- a maximum total senior leverage ratio of 3.0x; and
- a minimum fixed charge coverage ratio of 3.0x.

We intend to prepay the outstanding principal amount of term loans under our 2012 Term Loan Facility with the proceeds of the new notes offered hereby. See “Use of Proceeds”.

### **2017 Notes**

On February 2, 2007 Axtel issued US\$275.0 million of its 7.625% senior notes due 2017. These notes will mature on February 1, 2017. Interest is payable semi-annually on these notes. Beginning on or after February 1, 2012, we may redeem some or all of these notes.

### **2019 Notes**

On September 22, 2009 Axtel issued US\$300.0 million of its 9.0% senior notes due 2019 (referred to in this offering circular as the “existing notes”). The sale of the new notes in this offering will result in our having outstanding US\$490.0 million aggregate principal amount of 9.0% Senior Unsecured Notes due 2019. For more information concerning the existing notes, see “Description of the Notes.”

### **HP Operations Unsecured Promissory Notes**

Axtel signed promissory notes for an aggregate amount of US\$12.0 million in favor of HP Operations Mexico S. de R.L. de C.V. The term of these notes is for up to four years accruing at a competitive interest rate. Principal and interests are payable on a quarterly basis. The outstanding balance is US\$10.1 million as of December 31, 2009.

We intend to fund the principal installments due under such promissory notes in 2010 with the proceeds of the new notes offered hereby. See “Use of Proceeds.”

### **Cisco Systems Capital**

Axtel signed promissory notes for an aggregate amount of US\$27.7 million in favor of Cisco Systems Capital. The purpose is to finance Cisco Systems equipment. The tenor of these transactions is up to forty eight months with payments on a quarterly basis. The aggregate outstanding amount as of December 31, 2009 is approximately US\$19.2 million

We intend to fund the principal installments due under such promissory notes in 2010 with the proceeds of the new notes offered hereby. See “Use of Proceeds.”

### **Avantel-Telmex (Capital Lease Obligation)**

On January 2, 2006, Avantel and Telmex entered into a capacity lease agreement which provides Avantel the right to use certain telecommunications capacity and equipment. The amount registered in our balance sheet for this obligation is US\$21.5 million as of December 31, 2009.

We intend to fund the principal installments due under such lease agreement in 2010 with the proceeds of the new notes offered hereby. See “Use of Proceeds.”

#### **Banamex Promissory Note**

On January 15, 2010 Axtel executed a promissory notes for an aggregate amount of US\$32.0 million in favor of Banco Nacional de Mexico, S.A. The promissory note expires on July 14, 2010.

We intend to repay the principal amount and accrued interest under such promissory note with the proceeds of the new notes offered hereby. See “Use of Proceeds.”

#### **Other Indebtedness**

As of December 31, 2009 we had US\$23.7 million of other capital lease obligations.

We intend to fund the principal installments due under certain of these obligations in 2010, as well as certain other principal installments due in 2010, with the proceeds of the new notes offered hereby. See “Use of Proceeds.”

## DESCRIPTION OF THE NOTES

Axtel, S.A.B. de C.V. (the “Issuer”) previously issued US\$300.0 million in aggregate principal amount of 9.0% Senior Unsecured Notes due 2019 (the “Existing Notes”) under an indenture (the “Base Indenture”), dated September 22, 2009, among itself, the Subsidiary Guarantors and The Bank of New York Mellon, as Trustee. The Issuer will issue US\$190.0 million in aggregate principal amount of 9.0% Senior Unsecured Notes due 2019 (the “New Notes” and, together with the Existing Notes, the “Notes”) under the Base Indenture as supplemented by a supplemental indenture, to be entered into on March 22, 2010, by and among the Issuer, the Subsidiary Guarantors and the Trustee (the “Supplemental Indenture” and, together with the Base Indenture, the “Indenture”). The New Notes will be issued in a private transaction that is not subject to the registration requirements of the Securities Act. See “Transfer Restrictions.” The New Notes will constitute “Additional Notes” as such term is defined in the Indenture. Except as set forth herein, the terms of the New Notes will be substantially identical and include those stated in the Indenture and those made part of the Indenture by reference to the Trust Indenture Act. The New Notes offered and sold in offshore transactions under Regulation S will be issued and maintained during the distribution compliance period under a temporary CUSIP number. The terms of the New Notes include those stated in the Indenture and those made part of the Indenture by reference to the Trust Indenture Act.

Certain terms used in this description are defined under the subheading “—Certain Definitions.” In this description, the word “Company” refers only to Axtel, S.A.B. de C.V. and not to any of its subsidiaries. Capitalized terms used in this “Description of the Notes” are used in accordance with their respective definitions herein.

The following description is only a summary of the material provisions of the Indenture. We urge you to read the Indenture because it, not this description, defines your rights as Holders. Copies of the Indenture may be obtained from the Issuer upon request.

### Brief Description of the New Notes

The New Notes:

- are unsecured senior obligations of the Company;
- are senior in right of payment to any future Subordinated Obligations of the Company; and
- are guaranteed by each Subsidiary Guarantor.

### Principal, Maturity and Interest

The Company will issue the New Notes initially with a maximum aggregate principal amount of US\$190.0 million. The Company will issue the New Notes in denominations of US\$2,000 and any integral multiple of US\$1,000 in excess thereof. The New Notes will mature on September 22, 2019. Subject to our compliance with the covenant described under the subheading “—Certain Covenants—Limitation on Indebtedness,” we are entitled to, without the consent of the Holders, issue more notes under the Indenture on the same terms and conditions and with the same CUSIP numbers as the New Notes being offered hereby in an unlimited aggregate principal amount (the “Additional Notes”). The New Notes and the Additional Notes, if any, *provided* that such Additional Notes are treated as fungible with the New Notes for U.S. Federal income tax purposes, will be treated as a single class for all purposes of the Indenture, including waivers, amendments, redemptions and offers to purchase. Unless the context otherwise requires, for all purposes of the Indenture and this “Description of the Notes,” references to the Notes include any Additional Notes actually issued.

Interest on the New Notes will accrue at the rate of 9.0% per annum and will be payable semiannually in arrears on each March 22 and September 22, commencing on September 22, 2010. We will make each interest

payment to the Holders of record of the New Notes on the immediately preceding March 7 and September 7. We will pay interest on overdue principal at 1% per annum in excess of the above rate and will pay interest on overdue installments of interest at such higher rate to the extent lawful.

Interest on the New Notes will accrue from March 22, 2010. Interest will be computed on the basis of a 360-day year comprised of twelve 30-day months.

### Optional Redemption

Except as set forth below, we will not be entitled to redeem the Notes at our option prior to September 22, 2014.

On and after September 22, 2014, we will be entitled at our option to redeem all or a portion of the Notes upon not less than 30 nor more than 60 days' notice, at the redemption prices (expressed in percentages of principal amount on the redemption date), plus accrued interest to the redemption date (subject to the right of Holders of record on the relevant record date to receive interest due on the relevant interest payment date), if redeemed during the 12-month period commencing on September 22 of the years set forth below:

<u>Period</u>	<u>Redemption Price</u>
2014.....	104.500%
2015.....	103.000%
2016.....	101.500%
2017 and thereafter.....	100.000%

Prior to September 22, 2012, we may at our option on one or more occasions redeem Notes (which includes Additional Notes, if any) in an aggregate principal amount not to exceed 35% of the aggregate principal amount of the Notes (which includes Additional Notes, if any) originally issued prior to the redemption date at a redemption price (expressed as a percentage of principal amount) of 109%, plus accrued and unpaid interest to the redemption date, with the Net Cash Proceeds from one or more Equity Offerings; *provided, however*, that

- (1) at least 65% of such aggregate principal amount of Notes (which includes Additional Notes, if any) remains outstanding immediately after the occurrence of each such redemption (other than Notes held, directly or indirectly, by the Company or its Affiliates); and
- (2) each such redemption occurs within 90 days after the date of the related Equity Offering.

Prior to September 22, 2014, we will also be entitled at our option to redeem some or all of the Notes at a redemption price equal to 100% of the principal amount of the Notes plus the Applicable Premium as of, and accrued and unpaid interest to, the redemption date (subject to the right of Holders on the relevant record date to receive interest due on the relevant interest payment date). Notice of such redemption must be mailed by first-class mail to each Holder's registered address, not less than 30 nor more than 60 days prior to the redemption date.

"*Applicable Premium*" means with respect to a Note at any redemption date, the greater of (1) 1.00% of the principal amount of such Note on such redemption date and (2) the excess, if any, of (A) an amount equal to the present value at such redemption date of (i) the redemption price of such Note on September 22, 2014 (such redemption price being described in the second paragraph in this "—Optional Redemption" section exclusive of any accrued interest) plus (ii) all required remaining scheduled interest payments due on such Note (assuming that the interest rate per annum on the Notes applicable on the date on which the notice of redemption was given was in effect for the entire period) through September 22, 2014 (but excluding accrued and unpaid interest to the redemption date), computed using a discount rate equal to the Adjusted Treasury Rate, over (B) the principal amount of such Note on such redemption date.



“*Adjusted Treasury Rate*” means, with respect to any redemption date, (1) the yield, under the heading which represents the average for the immediately preceding week, appearing in the most recently published statistical release designated “H. 15(519)” or any successor publication which is published weekly by the Board of Governors of the Federal Reserve System and which establishes yields on actively traded United States Treasury securities adjusted to constant maturity under the caption “Treasury Constant Maturities” for the maturity corresponding to the Comparable Treasury Issue (if no maturity is within three months before or after September 22, 2014, yields for the two published maturities most closely corresponding to the Comparable Treasury Issue shall be determined and the Adjusted Treasury Rate shall be interpolated or extrapolated from such yields on a straight line basis, rounding to the nearest month) or (2) if such release (or any successor release) is not published during the week preceding the calculation date or does not contain such yields, the rate per year equal to the semi-annual equivalent yield to maturity of the Comparable Treasury Issue (expressed as a percentage of its principal amount) equal to the Comparable Treasury Price for such redemption date, in each case calculated on the third Business Day immediately preceding the redemption date, plus 0.50%.

“*Comparable Treasury Issue*” means, with respect to any redemption date, the United States Treasury security selected by the Quotation Agent as having a maturity comparable to the remaining term of the Notes from such redemption date to September 22, 2014, that would be utilized, at the time of selection and in accordance with customary financial practice, in pricing new issues of corporate debt securities of a maturity most nearly equal to September 22, 2014.

“*Comparable Treasury Price*” means, with respect to any redemption date, if clause (2) of the Adjusted Treasury Rate is applicable, the average of three, or such lesser number as is obtained by the Trustee, Reference Treasury Dealer Quotations for such redemption date.

“*Quotation Agent*” means the Reference Treasury Dealer selected by the Company.

“*Reference Treasury Dealer*” means Credit Suisse Securities (USA) LLC and Banc of America Securities LLC and their successors and assigns and two other nationally recognized investment banking firms selected by the Company that are primary U.S. Government securities dealers.

“*Reference Treasury Dealer Quotations*” means, with respect to each Reference Treasury Dealer and any redemption date, the average, as calculated by the Trustee, of the bid and asked prices for the Comparable Treasury Issue, expressed in each case as a percentage of its principal amount, quoted in writing to the Trustee by such Reference Treasury Dealer at 5:00 p.m., New York City time, on the third Business Day immediately preceding such redemption date.

### **Selection and Notice of Redemption**

If we are redeeming less than all the Notes at any time, the Trustee will select Notes on a pro rata basis, by lot or by such other method as the Trustee in its sole discretion shall deem to be fair and appropriate.

We will redeem the Notes of US\$1,000 or less in whole and not in part. We will cause notices of redemption to be mailed by first-class mail at least 30 but not more than 60 days before the redemption date to each Holder to be redeemed at its registered address.

If any Note is to be redeemed in part only, the notice of redemption that relates to that Note will state the portion of the principal amount thereof to be redeemed. We will issue a Note in a principal amount equal to the unredeemed portion of the original Note in the name of the Holder upon cancellation of the original Note. Notes called for redemption become due on the date fixed for redemption. On and after the redemption date, interest ceases to accrue on Notes or portions of them called for redemption.

## **Mandatory Redemption; Offers to Purchase; Open Market Purchases**

We are not required to make any mandatory redemption or sinking fund payments with respect to the Notes. However, under certain circumstances, we may be required to offer to purchase the Notes as described under the captions “—Change of Control” and “—Certain Covenants—Limitation on Sales of Assets and Subsidiary Stock.” We may at any time and from time to time purchase the Notes in the open market or otherwise.

## **Additional Amounts**

We and the Subsidiary Guarantors (the “payors”) are required to make all our payments under or with respect to the Notes free and clear of and without withholding or deduction for or on account of any present or future tax, duty, levy, impost, assessment or other governmental charge imposed or levied by Mexico or any political subdivision thereof or any jurisdiction in which a Subsidiary Guarantor is organized or a resident or any jurisdiction from which payments are made by the payor or its paying agent (each, a “Relevant Tax Jurisdiction”), including any penalties and interest related thereto (hereinafter “Taxes”), unless the relevant payor is required to withhold or deduct Taxes by law.

If any amount for or on account of Taxes is required to be withheld or deducted from any payment made under or with respect to the Notes, the payor will be required to pay such additional amounts (“Additional Amounts”) as may be necessary so that the net amount received by you (including Additional Amounts) after such withholding or deduction will not be less than the amount you would have received if such Taxes had not been withheld or deducted. However, no additional amounts will be paid for or on account of:

- (1) Taxes that would not have been imposed but for the fact that:
  - (A) the Holder has or had a present or former connection (or imputed connection) with a Relevant Tax Jurisdiction (including, without limitation, being resident, domiciled or a national of, or engaging in business or maintaining a permanent establishment in, or being physically present in a Relevant Tax Jurisdiction) other than by merely owning, or receiving payment under, the Notes;
  - (B) the Holder presented the Notes more than 30 days after the payment in question first became due and payable or the date on which payment thereof is duly provided for, whichever is later, except to the extent the Holder would have been entitled to the Additional Amounts if it had presented the Notes for payment during that 30 day period;
- (2) estate, inheritance, gift, sales, excise, transfer, personal property or similar Taxes;
- (3) Taxes payable otherwise than by withholding or deduction from payments of, or in respect of, principal of, or any premium or interest on, the Notes;
- (4) Taxes imposed or withheld because the Holder failed to comply with our reasonable request:
  - (A) to provide information concerning the nationality, residence, identity or address of the Holder; or
  - (B) to make any declaration or similar claim or satisfy any information or reporting requirement required by law, regulation, or other practice of a Relevant Tax Jurisdiction as a precondition to any exemption from all or part of any Taxes, but only to the extent the Holder is legally entitled to such exemption;
- (5) any Taxes imposed on a Holder to the extent imposed at a rate greater than the rate applicable to Holders generally because such Holder owns a specified percentage of our outstanding stock and/or because we own a specified percentage of the equity of such Holder; or
- (6) any combination of the items (1), (2), (3), (4) and (5) above.

Furthermore, no Additional Amounts will be paid with respect to any payment under the Notes to any Holder who is a fiduciary or partnership or any Person other than the sole beneficial owner of the payment, to the

extent the payment would, under the laws of the applicable Relevant Tax Jurisdiction, be treated as being derived or received for tax purposes by a beneficiary or settlor with respect to the fiduciary or a member of the partnership or a beneficial owner who would not have been entitled to the Additional Amounts had it been the Holder.

Upon request, a payor will provide the Trustee with official receipts or other documentation satisfactory to the Trustee evidencing the payment of the Taxes with respect to which Additional Amounts are paid.

Whenever in the Indenture there is mentioned, in any context:

- (1) the payment of principal;
- (2) purchase prices in connection with a purchase of the Notes;
- (3) interest; or
- (4) any other amount payable on or with respect to any of the Notes,

such reference shall be deemed to include payment of Additional Amounts as described under this heading to the extent that, in such context, Additional Amounts are, were or would be payable in respect thereof.

We will pay any present or future stamp, documentary or other similar excise taxes, governmental charges or levies that arise in a Relevant Tax Jurisdiction from the execution, delivery, enforcement or registration of the Notes, the Indenture or any other document or instrument related to them (including, without limitation, any such Taxes that are referred to as “court” or “property” Taxes), and we will agree to indemnify the Holders for any such Taxes paid by such Holders.

The obligations described under this heading will survive any termination, defeasance or discharge of the Indenture and will apply mutatis mutandis to any jurisdiction in which any successor Person to a payor is organized or any political subdivision or taxing authority or agency thereof or therein.

For a discussion of Mexican withholding taxes applicable to payments under or with respect to the Notes, see “Certain United States Federal Income Tax Consequences” and “Material Mexican Tax Consequences.”

### **Redemption for Changes in Withholding Taxes**

The Company may redeem the Notes in whole, but not in part, upon giving not less than 30 nor more than 60 days’ prior notice mailed by first class mail to each Holder’s registered address, at 100% of their principal amount, plus accrued and unpaid interest to the redemption date (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date) and including Additional Amounts payable in respect of such payment, if (i) the Company certifies to the Trustee immediately prior to the giving of such notice that as a result of any change in or amendment to the laws, regulations, general rules or treaties of a Relevant Tax Jurisdiction, or any change in the application or official interpretation of such laws, regulations, general rules or treaties, which change or amendment is announced and becomes effective after September 22, 2009 (or, if the applicable Relevant Tax Jurisdiction first became a Relevant Tax Jurisdiction after September 22, 2009 as a result of a merger of the Company into a successor entity, which change or amendment is announced and becomes effective after the effective date of such merger) the Company has become or will become obligated to pay Additional Amounts with respect to the Notes; *provided* that the Company shall have no right to redeem the Notes as a result of a change in Mexican tax law unless the rate of Mexican withholding tax giving rise to such Additional Amounts exceeds 4.9% and (ii) such obligations cannot be avoided by the Company taking reasonable measures available to it; *provided*, however, that (a) no such notice of redemption will be given earlier than 60 days prior to the earliest date on which the Company would be obligated to pay such Additional Amounts and (b) at the time such notice is given, the Company’s obligation to pay such Additional Amounts remains in effect. Prior to giving of any notice of redemption described in this paragraph, the Company

will deliver to the Trustee an Officers' Certificate stating that the Company is entitled to effect such redemption in accordance with the terms set forth in the Indenture and setting forth in reasonable detail a statement of the facts relating thereto (together with a written Opinion of Counsel to the effect that the Company has become obligated to pay such Additional Amounts as a result of a change or amendment described above and that all governmental approvals necessary for the Company to effect such redemption have been obtained and are in full force and effect or specifying any such necessary approvals that as of the date of such opinion have not been obtained).

## **Guarantees**

The Subsidiary Guarantors will jointly and severally guarantee, on a senior unsecured basis, our obligations under the Notes and the Indenture. The Subsidiary Guarantors include all of our Restricted Subsidiaries existing on September 22, 2009 and will include any of our future Restricted Subsidiaries. The obligations of each Subsidiary Guarantor under its Subsidiary Guaranty will be limited as necessary to prevent that Subsidiary Guaranty from constituting a fraudulent conveyance under applicable law. See "Risk Factors—Risks Relating to the New Notes—It is possible that the Guarantees by our subsidiaries may not be enforceable."

Each Subsidiary Guarantor that makes a payment under its Subsidiary Guaranty will be entitled upon payment in full of all guaranteed obligations under the Indenture to a contribution from each other Subsidiary Guarantor in an amount equal to such other Subsidiary Guarantor's pro rata portion of such payment based on the respective net assets of all the Subsidiary Guarantors at the time of such payment determined in accordance with GAAP.

If a Subsidiary Guaranty were rendered voidable, it could be subordinated by a court to all other indebtedness (including guarantees and other contingent liabilities) of the applicable Subsidiary Guarantor, and, depending on the amount of such indebtedness, a Subsidiary Guarantor's liability on its Subsidiary Guaranty could be reduced to zero. See "Risk Factors—It is possible that the Guarantees by our subsidiaries may not be enforceable."

Pursuant to the Indenture, (A) a Subsidiary Guarantor may consolidate with, merge with or into, or transfer all or substantially all its assets to any other Person to the extent described below under "—Certain Covenants—Merger and Consolidation" and (B) the Capital Stock of a Subsidiary Guarantor may be sold or otherwise disposed of to another Person to the extent described below under "—Certain Covenants—Limitation on Sales of Assets and Subsidiary Stock"; *provided, however*, that in the case of the consolidation, merger or transfer of all or substantially all the assets of such Subsidiary Guarantor, if such other Person is not the Company or a Subsidiary Guarantor, such Subsidiary Guarantor's obligations under its Subsidiary Guaranty must be expressly assumed by supplemental indenture or by such other Person, except that such assumption will not be required in the case of:

- (1) the sale or other disposition (including by way of consolidation or merger) of a Subsidiary Guarantor, including the sale or disposition of Capital Stock of a Subsidiary Guarantor following which such Subsidiary Guarantor is no longer a Subsidiary; or
- (2) the sale or disposition of all or substantially all the assets of a Subsidiary Guarantor;

in each case other than to the Company or an Affiliate of the Company and as permitted by the Indenture. Upon any sale or disposition described in clause (1) or (2) above, the obligor on the related Subsidiary Guaranty will be released from its obligations thereunder.

The Subsidiary Guaranty of a Subsidiary Guarantor also will be released:

- (1) upon the designation of such Subsidiary Guarantor as an Unrestricted Subsidiary;
- (2) at such time as such Subsidiary Guarantor does not have any Indebtedness outstanding that would have required such Subsidiary Guarantor to enter into a Guaranty Agreement pursuant to the covenant described under “—Certain Covenants—Future Guarantors”; or
- (3) if we exercise our legal defeasance option or our covenant defeasance option as described under “—Defeasance.”

## **Ranking**

### *Senior Indebtedness versus New Notes*

The indebtedness evidenced by the Notes and the Subsidiary Guaranties will be unsecured and will rank *pari passu* in right of payment to the Senior Indebtedness of the Company and the Subsidiary Guarantors, as the case may be. The Notes will be guaranteed by the Subsidiary Guarantors.

As of December 31, 2009, on an as adjusted basis after giving effect to the Refinancings and the issuance of the New Notes:

- (1) the Company’s Senior Indebtedness was approximately US\$822.7 million, including US\$12.0 million of secured indebtedness; and
- (2) the Subsidiary Guarantors’ Indebtedness was approximately US\$2.1 million.

The Notes are unsecured obligations of the Company. Secured debt and other secured obligations of the Company will be effectively senior to the Notes to the extent of the value of the assets securing such debt or other obligations.

### *Liabilities of Subsidiaries versus New Notes*

A substantial portion of our operations is conducted through our Subsidiaries. Any right we have to receive the assets of any such Subsidiary upon such Subsidiary’s liquidation or reorganization (and the consequent right of the Holders to participate in the distribution of the proceeds of those assets) effectively will be subordinated by operation of law to the claims of such Subsidiary’s creditors (including trade creditors) and holders of its Preferred Stock, except to the extent that such Subsidiaries guarantee our obligations under the Notes, and except to the extent that we are recognized as a creditor or preferred stockholder of such Subsidiary, in which case our claims would still be subordinate to any indebtedness or Preferred Stock of such Subsidiary senior in right of payment to that held by us.

As of the issue date of the New Notes, all our continuing existing Subsidiaries, other than Telecom Networks, Inc., will be Subsidiary Guarantors. Although the Indenture limits the incurrence of Indebtedness and Preferred Stock of certain of our Subsidiaries, such limitation is subject to a number of significant qualifications. Moreover, the Indenture does not impose any limitation on the incurrence by such subsidiaries of liabilities that are not considered Indebtedness under the Indenture. See “—Certain Covenants—Limitation on Indebtedness.”

## **Book-Entry; Delivery and Form**

The New Notes are being offered and sold to qualified institutional buyers in reliance on Rule 144A (“Rule 144A Notes”). New Notes also may be offered and sold in offshore transactions in reliance on Regulation S (“Regulation S Notes”). Except as set forth below, New Notes will be issued in registered, global form in minimum denominations of US\$2,000 and integral multiples of US\$1,000 in excess of US\$2,000. New Notes will be issued at the closing of this offering only against payment in immediately available funds.

Rule 144A Notes initially will be represented by one or more global New Notes in registered form without interest coupons (collectively, the “Rule 144A Global Notes”). Regulation S Notes initially will be represented by one or more global notes in registered form without interest coupons (collectively, the “Regulation S Global Notes”). The Rule 144A Global Notes and the Regulation S Global Notes are collectively referred to herein as the “Global Notes.” The Global Notes will be deposited upon issuance with the Trustee as custodian for The Depository Trust Company (“DTC”), in New York, New York, and registered in the name of DTC or its nominee, in each case for credit to an account of a direct or indirect participant in DTC as described below. Beneficial interests in the Rule 144A Global Notes may not be exchanged for beneficial interests in the Regulation S Global Notes at any time except in the limited circumstances described below. See “—Exchanges Among Global Notes.”

Except as set forth below, the Global Notes may be transferred, in whole and not in part, only to another nominee of DTC or to a successor of DTC or its nominee. Beneficial interests in the Global Notes may not be exchanged for New Notes in certificated form except in the limited circumstances described below. See “—Exchange of Global Notes for Certificated Notes.”

Rule 144A Notes (including beneficial interests in the Rule 144A Global Notes) will be subject to certain restrictions on transfer and will bear a restrictive legend as described under “Transfer Restrictions.” Regulation S Notes will also be subject to certain restrictions on transfer and will bear the legend as described under “Transfer Restrictions.” In addition, transfers of beneficial interests in the Global Notes will be subject to the applicable rules and procedures of DTC and its direct or indirect Participants, which may change from time to time.

### **Depository Procedures**

The following description of the operations and procedures of DTC is provided solely as a matter of convenience. These operations and procedures are solely within the control of the respective settlement systems and are subject to changes by them. We take no responsibility for these operations and procedures and urge investors to contact the system or their participants directly to discuss these matters.

DTC has advised us that DTC is a limited-purpose trust company organized under the laws of the State of New York, a “banking organization” within the meaning of New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the Uniform Commercial Code and a “clearing agency” registered pursuant to the provisions of Section 17A of the Exchange Act. DTC was created to hold securities for its participating organizations (collectively, the “Participants”) and to facilitate the clearance and settlement of transactions in those securities between Participants through electronic book-entry changes in accounts of its Participants. The Participants include securities brokers and dealers (including the initial purchasers), banks, trust companies, clearing corporations and certain other organizations. Access to DTC’s system is also available to other entities such as banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a Participant, either directly or indirectly (collectively, the “Indirect Participants”). Persons who are not Participants may beneficially own securities held by or on behalf of DTC only through the Participants or the Indirect Participants. The ownership interests in, and transfers of ownership interests in, each security held by or on behalf of DTC are recorded on the records of the Participants and Indirect Participants.

DTC has also advised us that, pursuant to procedures established by it:

- (1) upon deposit of the Global Notes, DTC will credit the accounts of Participants designated by the Initial Purchasers with portions of the principal amount of the Global Notes; and
- (2) ownership of these interests in the Global Notes will be shown on, and the transfer of ownership of these interests will be effected only through, records maintained by DTC (with respect to the Participants) or by the Participants and the Indirect Participants (with respect to other owners of beneficial interests in the Global Notes).



Investors in the Global Notes who are Participants in DTC's system may hold their interests therein directly through DTC. Investors in the Global Notes who are not Participants may hold their interests therein indirectly through organizations which are Participants in such system. All interests in a Global Note may be subject to the procedures and requirements of DTC. The laws of some states require that certain Persons take physical delivery in definitive form of securities that they own. Consequently, the ability to transfer beneficial interests in a Global Note to such Persons will be limited to that extent. Because DTC can act only on behalf of Participants, which in turn act on behalf of Indirect Participants, the ability of a Person having beneficial interests in a Global Note to pledge such interests to Persons that do not participate in the DTC system, or otherwise take actions in respect of such interests, may be affected by the lack of a physical certificate evidencing such interests.

**Except as described below, owners of an interest in the Global Notes will not have New Notes registered in their names, will not receive physical delivery of New Notes in certificated form and will not be considered the registered owners or "Holders" thereof under the Indenture for any purpose.**

Payments in respect of the principal of, and interest and premium and additional interest, if any, on a Global Note registered in the name of DTC or its nominee will be payable to DTC in its capacity as the registered Holder under the Indenture. Under the terms of the Indenture, the Company and the Trustee will treat the Persons in whose names the New Notes, including the Global Notes, are registered as the owners of the New Notes for the purpose of receiving payments and for all other purposes. Consequently, neither the Company, the Trustee nor any agent of the Company or the Trustee has or will have any responsibility or liability for:

- (1) any aspect of DTC's records or any Participant's or Indirect Participant's records relating to or payments made on account of beneficial ownership interest in the Global Notes or for maintaining, supervising or reviewing any of DTC's records or any Participant's or Indirect Participant's records relating to the beneficial ownership interests in the Global Notes; or
- (2) any other matter relating to the actions and practices of DTC or any of its Participants or Indirect Participants.

DTC has advised us that its current practice, upon receipt of any payment in respect of securities such as the New Notes (including principal and interest), is to credit the accounts of the relevant Participants with the payment on the payment date unless DTC has reason to believe it will not receive payment on such payment date. Each relevant Participant is credited with an amount proportionate to its beneficial ownership of an interest in the principal amount of the relevant security as shown on the records of DTC. Payments by the Participants and the Indirect Participants to the beneficial owners of Notes will be governed by standing instructions and customary practices and will be the responsibility of the Participants or the Indirect Participants and will not be the responsibility of DTC, the Trustee or the Company. Neither the Company nor the Trustee will be liable for any delay by DTC or any of its Participants in identifying the beneficial owners of the Notes, and the Company and the Trustee may conclusively rely on and will be protected in relying on instructions from DTC or its nominee for all purposes.

Subject to the transfer restrictions set forth under "Transfer Restrictions," transfers between Participants in DTC will be effected in accordance with DTC's procedures, and will be settled in same-day funds.

DTC has advised the Company that it will take any action permitted to be taken by a Holder only at the direction of one or more Participants to whose account DTC has credited the interests in the Global Notes and only in respect of such portion of the aggregate principal amount of the Notes as to which such Participant or Participants has or have given such direction. However, if there is an Event of Default under the New Notes, DTC reserves the right to exchange the Global Notes for legended New Notes in certificated form, and to distribute such Notes to its Participants.

Neither the Company nor the Trustee nor any of their respective agents will have any responsibility for the performance by DTC or its direct or indirect Participants of their respective obligations under the rules and procedures governing their operations.

### **Exchange of Global Notes for Certificated Notes**

A Global Note is exchangeable for Certificated Notes if:

- (1) DTC (a) notifies the Issuer that it is unwilling or unable to continue as depository for the Global Notes and DTC fails to appoint a successor depository or (b) has ceased to be a clearing agency registered under the Exchange Act; or
- (2) there has occurred and is continuing a Default with respect to the Notes.

In addition, beneficial interests in a Global Note may be exchanged for Certificated Notes upon prior written notice given to the Trustee by or on behalf of DTC in accordance with the Indenture. In all cases, Certificated Notes delivered in exchange for any Global Note or beneficial interests in Global Notes will be registered in the names, and issued in any approved denominations, requested by or on behalf of the depository (in accordance with its customary procedures) and will bear the applicable restrictive legend referred to in “Transfer Restrictions,” unless that legend is not required by applicable law.

### **Exchange of Certificated Notes for Global Notes**

Certificated Notes may not be exchanged for beneficial interests in any Global Note unless the transferor first delivers to the Trustee a written certificate (in the form provided in the Indenture) to the effect that such transfer will comply with the appropriate transfer restrictions applicable to such Notes. See “Transfer Restrictions.”

### **Exchanges Among Global Notes**

Beneficial interests in the Regulation S Global Note may be exchanged for beneficial interests in the Rule 144A Global Note prior to the expiration of the 40-day “distribution compliance period” as defined in Regulation S under the Securities Act (the “Distribution Compliance Period”) only upon certification in form reasonably satisfactory to the Trustee to the effect that such transfer is made pursuant to Rule 144A to a “qualified institutional buyer” (as defined in Rule 144A under the Securities Act).

Beneficial interest in a Rule 144A Global Note may be transferred to a Person who takes delivery in the form of an interest in the Regulation S Global Note, whether before or after the expiration of the Distribution Compliance Period, only if the transferor first delivers to the Trustee a written certificate (in the form provided in the Indenture) to the effect that such transfer is being made in accordance with Rule 903 or 904 of Regulation S or Rule 144.

Transfers involving exchanges of beneficial interests between the Regulation S Global Notes and the Rule 144A Global Notes will be effected in DTC by means of an instruction originated by the Trustee through the DTC Deposit/Withdraw at Custodian system. Accordingly, in connection with any such transfer, appropriate adjustments will be made to reflect changes in the principal amounts of the Regulation S Global Note and the Rule 144A Global Note, as applicable. Any beneficial interest in one of the Global Notes that is transferred to a Person who takes delivery in the form of an interest in the other Global Note will, upon transfer, cease to be an interest in such Global Note and will become an interest in the other Global Note and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to beneficial interest in such other Global Note for so long as it remains such an interest.

### **Same Day Settlement and Payment**

The Issuer will make payments in respect of the Notes represented by the Global Notes (including principal, premium, if any, interest and additional interest, if any) by wire transfer of immediately available funds to the accounts specified by the Global Note Holder. The Issuer will make all payments of principal, interest and premium and additional interest, if any, with respect to Certificated Notes by wire transfer of immediately available funds to the accounts specified by the Holders of the Certificated Notes or, if no such account is

specified, by mailing a check to each such Holder's registered address. The Notes represented by the Global Notes are expected to trade in DTC's Same-Day Funds Settlement System, and any permitted secondary market trading activity in such Notes will, therefore, be required by DTC to be settled in immediately available funds. The Issuer expect that secondary trading in any Certificated Notes will also be settled in immediately available funds.

### **Change of Control**

Upon the occurrence of any of the following events (each a "Change of Control"), each Holder shall have the right to require that the Company repurchase such Holder's Notes at a purchase price in cash equal to 101% of the principal amount thereof on the date of purchase plus accrued and unpaid interest, if any, to the date of purchase (subject to the right of holders of record on the relevant record date to receive interest due on the relevant interest payment date):

- (1) any "person" (as such term is used in Sections 13(d) and 14(d) of the Exchange Act), other than one or more Permitted Holders, is or becomes the beneficial owner (as defined in Rules 13d-3 and 13d-5 under the Exchange Act, except that for purposes of this clause (1), (x) such person shall be deemed to have "beneficial ownership" of all shares that any such person has the right to acquire, whether such right is exercisable immediately or only after the passage of time and (y) such person shall not be deemed to have "beneficial ownership" of any shares solely as a result of a voting or similar agreement entered into in connection with a merger agreement or asset sale agreement), directly or indirectly, of more than 35% of the total voting power of the Voting Stock of the Company; *provided, however*, that Permitted Holders beneficially own (as defined in Rules 13d-3 and 13d-5 under the Exchange Act), directly or indirectly, in the aggregate a lesser percentage of the total voting power of the Voting Stock of the Company than such other person and do not have the right or ability by voting power, contract or otherwise to elect or designate for election a majority of the Board of Directors (for the purposes of this clause (1), such other person shall be deemed to beneficially own any Voting Stock of the Company held by any other person (a "parent entity"), if such other person is the beneficial owner (as defined in this clause (1)), directly or indirectly, of more than 35% of the voting power of the Voting Stock of such parent entity and the Permitted Holders beneficially own (as defined in this clause (1)), directly or indirectly, in the aggregate a lesser percentage of the voting power of the Voting Stock of such parent entity and do not have the right or ability by voting power, contract or otherwise to elect or designate for election a majority of the board of directors of such parent entity);
- (2) individuals who on September 22, 2009 constituted the Board of Directors (together with any new directors whose election by such Board of Directors or whose appointment or nomination for election by the shareholders of the Company was approved by a vote of a majority of the directors of the Company then still in office who were either directors on September 22, 2009 or whose appointment, election or nomination for election was approved by the Permitted Holders or by directors previously so approved) cease for any reason to constitute a majority of the Board of Directors then in office;
- (3) the adoption of a plan relating to the liquidation or dissolution of the Company; *provided, however*, that this clause (3) will not be applicable to (A) a Restricted Subsidiary consolidating with, merging into or transferring all or part of its properties and assets to the Company or (B) the Company merging with an Affiliate of the Company solely for the purpose and with the sole effect of reincorporating the Company in another jurisdiction; or
- (4) the merger or consolidation of the Company with or into another Person or the merger of another Person with or into the Company, or the sale of all or substantially all the assets of the Company (determined on a consolidated basis) to another Person other than a transaction in which holders of securities that represented 100% of the Voting Stock of the Company immediately prior to such transaction (or other securities into which such securities are converted as part of such merger or consolidation transaction) own directly or indirectly at least a majority of the voting power of the Voting Stock of the transferee Person or surviving Person in such merger or consolidation transaction immediately after such transaction.

Within 30 days following any Change of Control, we will mail a notice to each Holder with a copy to the Trustee (the “Change of Control Offer”) stating:

- (1) that a Change of Control has occurred and that such Holder has the right to require us to purchase such Holder’s Notes at a purchase price in cash equal to 101% of the principal amount thereof on the date of purchase, plus accrued and unpaid interest, if any, to the date of purchase (subject to the right of Holders of record on the relevant record date to receive interest on the relevant interest payment date);
- (2) the circumstances and relevant facts regarding such Change of Control (including information with respect to *pro forma* historical income, cash flow and capitalization, in each case after giving effect to such Change of Control);
- (3) the purchase date (which shall be no earlier than 30 days nor later than 60 days from the date such notice is mailed); and
- (4) the instructions, as determined by us, consistent with the covenant described hereunder, that a Holder must follow in order to have its Notes purchased.

We will not be required to make a Change of Control Offer following a Change of Control if a third party makes the Change of Control Offer in the manner, at the times and otherwise in compliance with the requirements set forth in the Indenture applicable to a Change of Control Offer made by us and purchases all Notes validly tendered and not withdrawn under such Change of Control Offer.

We will comply, to the extent applicable, with the requirements of Section 14(e) of the Exchange Act and any other securities laws or regulations in connection with the repurchase of Notes as a result of a Change of Control. To the extent that the provisions of any securities laws or regulations conflict with the provisions of the covenant described hereunder, we will comply with the applicable securities laws and regulations and shall not be deemed to have breached our obligations under the covenant described hereunder by virtue of our compliance with such securities laws or regulations.

The Change of Control purchase feature of the Notes may in certain circumstances make more difficult or discourage a sale or takeover of the Company and, thus, the removal of incumbent management. The Change of Control purchase feature is a result of negotiations between the Company and the Initial Purchasers. We have no present intention to engage in a transaction involving a Change of Control, although it is possible that we could decide to do so in the future. Subject to the limitations discussed below, we could, in the future, enter into certain transactions, including acquisitions, refinancings or other recapitalizations, that would not constitute a Change of Control under the Indenture, but that could increase the amount of indebtedness outstanding at such time or otherwise affect our capital structure or credit ratings. Restrictions on our ability to Incur additional Indebtedness are contained in the covenants described under “—Certain Covenants—Limitation on Indebtedness,” “—Limitation on Liens” and “—Limitation on Sale/Leaseback Transactions.” Such restrictions can only be waived with the consent of the Holders of a majority in principal amount of the Notes then outstanding. Except for the limitations contained in such covenants, however, the Indenture will not contain any covenants or provisions that may afford Holders protection in the event of a highly leveraged transaction.

The Existing Term Loan Agreement and certain future indebtedness that we may incur may contain prohibitions on the occurrence of certain events that would constitute a Change of Control or require the repurchase of such indebtedness upon a Change of Control. Moreover, the exercise by the Holders of their right to require us to repurchase their Notes could cause a default under such indebtedness, even if the Change of Control itself does not, due to the financial effect of such repurchase on us. Finally, our ability to pay cash to the Holders following the occurrence of a Change of Control may be limited by our then existing financial resources. There can be no assurance that sufficient funds will be available when necessary to make any required repurchases.

The definition of “Change of Control” includes a disposition of all or substantially all of the assets of the Company to any Person. Although there is a limited body of case law interpreting the phrase “substantially all,”

there is no precise established definition of the phrase under applicable law. Accordingly, in certain circumstances there may be a degree of uncertainty as to whether a particular transaction would involve a disposition of “all or substantially all” of the assets of the Company. As a result, it may be unclear as to whether a Change of Control has occurred and whether a Holder may require the Company to make an offer to repurchase the Notes as described above.

The provisions under the Indenture relative to our obligation to make an offer to repurchase the Notes as a result of a Change of Control may be waived or modified with the written consent of the Holders of a majority in principal amount of the Notes.

### **Certain Covenants**

The Indenture contains covenants including, among others, the following:

#### ***Limitation on Indebtedness***

(a) The Company will not, and will not permit any Restricted Subsidiary to, Incur, directly or indirectly, any Indebtedness; *provided, however*, that the Company and the Subsidiary Guarantors will be entitled to Incur Indebtedness if, on the date of such Incurrence and after giving effect thereto on a *pro forma* basis the Consolidated Leverage Ratio would be less than 4.0 to 1.

(b) Notwithstanding the foregoing paragraph (a), the Company and the Restricted Subsidiaries will be entitled to Incur any or all of the following Indebtedness:

- (1) Indebtedness owed to and held by the Company or a Wholly Owned Subsidiary; *provided, however*, that (A) any subsequent issuance or transfer of any Capital Stock which results in any such Wholly Owned Subsidiary ceasing to be a Wholly Owned Subsidiary or any subsequent transfer of such Indebtedness (other than to the Company or a Wholly Owned Subsidiary) shall be deemed, in each case, to constitute the Incurrence of such Indebtedness by the obligor thereon, (B) if the Company is the obligor on such Indebtedness, such Indebtedness is expressly subordinated to the prior payment in full in cash of all obligations with respect to the Notes, and (C) if a Subsidiary Guarantor is the obligor on such Indebtedness, such Indebtedness is expressly subordinated to the prior payment in full in cash of all obligations of such obligor with respect to its Subsidiary Guaranty;
- (2) the Existing Notes (other than any Additional Notes, excluding the New Notes);
- (3) Indebtedness outstanding on September 22, 2009 (other than Indebtedness described in clause (1) or (2) of this covenant);
- (4) Refinancing Indebtedness in respect of Indebtedness Incurred pursuant to paragraph (a) or pursuant to clause (2) or (3) or this clause;
- (5) Hedging Obligations consisting of (x) Interest Rate Agreements directly related to Indebtedness permitted to be Incurred by the Company and its Restricted Subsidiaries pursuant to the Indenture or (y) Hedging Obligations relating to Currency Agreements provided such Currency Agreements are entered into for bona fide hedging purposes of the Company or any Restricted Subsidiary and not for the purpose of speculation;
- (6) obligations in respect of performance, bid and surety bonds and completion guarantees provided by the Company or any Restricted Subsidiary in the ordinary course of business, including guarantees or obligations of the Company or any Restricted Subsidiary with respect to letters of credit and/or fianzas supporting such bid, performance or surety obligations;
- (7) Indebtedness arising from the honoring by a bank or other financial institution of a check, draft or similar instrument drawn against insufficient funds in the ordinary course of business; *provided, however*, that such Indebtedness is extinguished within two Business Days of its Incurrence;



- (8) Purchase Money Obligations and Capital Lease Obligations, in an aggregate principal amount at any time outstanding not exceeding an amount equal to 10% of Consolidated Total Assets at any time outstanding;
- (9) Indebtedness consisting of the Subsidiary Guaranty of a Subsidiary Guarantor and any Guarantee by a Subsidiary Guarantor of Indebtedness Incurred pursuant to paragraph (a) or pursuant to clause (1), (2), (3) or pursuant to clause (4) to the extent the Refinancing Indebtedness Incurred thereunder directly or indirectly Refinances Indebtedness Incurred pursuant to paragraph (a) or pursuant to clause (2) or (3);
- (10) indemnification, adjustment of purchase price, earn-out or similar obligations, in each case, incurred or assumed in connection with the acquisition or disposition of any business or assets of the Company or any Restricted Subsidiary or Capital Stock of a Restricted Subsidiary, other than guarantees of Indebtedness incurred by any Person acquiring all or any portion of such business, assets or equity interests for the purposes of financing or in contemplation of any such acquisition; *provided* that (a) any amount of such obligations included on the face of the balance sheet of the Company or any Restricted Subsidiary shall not be permitted under this clause (10) and (b) in the case of a disposition, the maximum aggregate liability in respect of all such obligations outstanding under this clause (10) shall at no time exceed the gross proceeds actually received by the Issuer and the Restricted Subsidiaries in connection with such disposition; and
- (11) Indebtedness of the Company or of any of its Restricted Subsidiaries in an aggregate principal amount which, when taken together with all other Indebtedness of the Company and its Restricted Subsidiaries outstanding on the date of such Incurrence (other than Indebtedness permitted by clauses (1) through (10) above or paragraph (a)) does not exceed US\$30 million.

(c) Notwithstanding the foregoing, neither the Company nor any Subsidiary Guarantor will Incur any Indebtedness pursuant to the foregoing paragraph (b) if the proceeds thereof are used, directly or indirectly, to Refinance any Subordinated Obligations of the Company or any Subsidiary Guarantor unless such Indebtedness shall be subordinated to the Notes or the applicable Subsidiary Guaranty to at least the same extent as such Subordinated Obligations.

(d) For purposes of determining compliance with this covenant:

- (1) in the event that an item of Indebtedness (or any portion thereof) meets the criteria of more than one of the types of Indebtedness described above, the Company, in its sole discretion, will classify such item of Indebtedness (or any portion thereof) at the time of Incurrence and will only be required to include the amount and type of such Indebtedness in one of the above clauses; and
- (2) the Company will be entitled to divide and classify an item of Indebtedness in more than one of the types of Indebtedness described above.

(e) For purposes of determining compliance with any US dollar denominated restriction on the Incurrence of Indebtedness where the Indebtedness Incurred is denominated in a different currency, the amount of such Indebtedness will be the US Dollar Equivalent determined on the date of the Incurrence of such Indebtedness; *provided, however*, that if any such Indebtedness denominated in a different currency is subject to a Currency Agreement with respect to US dollars covering all principal, premium, if any, and interest payable on such Indebtedness, the amount of such Indebtedness expressed in US dollars will be as provided in such Currency Agreement. The principal amount of any Refinancing Indebtedness Incurred in the same currency as the Indebtedness being Refinanced will be the U.S. Dollar Equivalent of the Indebtedness Refinanced, except to the extent that (1) such US Dollar Equivalent was determined based on a Currency Agreement, in which case the Refinancing Indebtedness will be determined in accordance with the preceding sentence, and (2) the principal amount of the Refinancing Indebtedness exceeds the principal amount of the Indebtedness being Refinanced, in which case the US Dollar Equivalent of such excess will be determined on the date such Refinancing Indebtedness is Incurred.



### ***Limitation on Restricted Payments***

(a) The Company will not, and will not permit any Restricted Subsidiary, directly or indirectly, to make a Restricted Payment if at the time the Company or such Restricted Subsidiary makes such Restricted Payment:

- (1) a Default shall have occurred and be continuing (or would result therefrom);
  - (2) the Company is not entitled to Incur an additional US\$1.00 of Indebtedness pursuant to paragraph (a) of the covenant described under “—Limitation on Indebtedness”; or
  - (3) the aggregate amount of such Restricted Payment and all other Restricted Payments since September 22, 2009 (other than Restricted Payments made pursuant to clauses (1), (2), (4), (5), (6), (7) or (9) of the next paragraph) would exceed the sum of (without duplication):
    - (A) 50% of the Adjusted Consolidated Net Income accrued during the period (treated as one accounting period) beginning on April 1, 2009, to the end of the most recent fiscal quarter ending at least 45 days prior to the date of such Restricted Payment (or, in case such Adjusted Consolidated Net Income shall be a deficit, minus 100% of such deficit); plus
    - (B) 100% of the aggregate Net Cash Proceeds received by the Company from the issuance or sale of its Capital Stock (other than Disqualified Stock) subsequent to September 22, 2009 (other than an issuance or sale to a Subsidiary of the Company and other than an issuance or sale to an employee stock ownership plan or to a trust established by the Company or any of its Subsidiaries for the benefit of their employees) and 100% of any cash capital contribution received by the Company from its shareholders subsequent to September 22, 2009; plus
    - (C) the amount by which Indebtedness of the Company is reduced on the Company’s balance sheet upon the conversion or exchange (other than by a Subsidiary of the Company) subsequent to September 22, 2009 of any Indebtedness of the Company convertible or exchangeable for Capital Stock (other than Disqualified Stock) of the Company (less the amount of any cash, or the fair value of any other property, distributed by the Company upon such conversion or exchange); *provided, however*, that the foregoing amount shall not exceed the Net Cash Proceeds received by the Company or any Restricted Subsidiary from the sale of such Indebtedness (excluding Net Cash Proceeds from sales to a Subsidiary of the Company or to an employee stock ownership plan or to a trust established by the Company or any of its Subsidiaries for the benefit of their employees); plus
    - (D) an amount equal to the sum of (i) the net reduction in the Investments (other than Permitted Investments) made by the Company or any Restricted Subsidiary in any Person resulting from repurchases, repayments or redemptions of such Investments by such Person, proceeds realized on the sale of such Investment and proceeds representing the return of capital (excluding dividends and distributions), in each case received by the Company or any Restricted Subsidiary, and (ii) to the extent such Person is an Unrestricted Subsidiary, the portion (proportionate to the Company’s equity interest in such Subsidiary) of the fair market value of the net assets of such Unrestricted Subsidiary at the time such Unrestricted Subsidiary is designated a Restricted Subsidiary; *provided, however*, that the foregoing sum shall not exceed, in the case of any such Person or Unrestricted Subsidiary, the amount of Investments (excluding Permitted Investments) previously made (and treated as a Restricted Payment) by the Company or any Restricted Subsidiary in such Person or Unrestricted Subsidiary.
- (b) The preceding provisions will not prohibit:
- (1) any Restricted Payment made out of the Net Cash Proceeds of the substantially concurrent sale of, or made by exchange for, Capital Stock of the Company (other than Disqualified Stock and other than Capital Stock issued or sold to a Subsidiary of the Company or an employee stock ownership plan or to a trust established by the Company or any of its Subsidiaries for the benefit of their employees) or a

substantially concurrent cash capital contribution received by the Company from its shareholders; *provided, however*, that (A) such Restricted Payment shall be excluded in the calculation of the amount of Restricted Payments and (B) the Net Cash Proceeds from such sale or such cash capital contribution (to the extent so used for such Restricted Payment) shall be excluded from the calculation of amounts under clause (3)(B) of paragraph (a) above;

- (2) any purchase, repurchase, redemption, defeasance or other acquisition or retirement for value of Subordinated Obligations of the Company or a Subsidiary Guarantor made by exchange for, or out of the proceeds of the substantially concurrent sale of, Indebtedness of such Person which is permitted to be Incurred pursuant to the covenant described under “—Limitation on Indebtedness”; *provided, however*, that such purchase, repurchase, redemption, defeasance or other acquisition or retirement for value shall be excluded in the calculation of the amount of Restricted Payments;
- (3) dividends paid within 60 days after the date of declaration thereof if at such date of declaration such dividend would have complied with this covenant; *provided, however*, that at the time of payment of such dividend, no other Default shall have occurred and be continuing (or result therefrom); *provided further, however*, that such dividend shall be included in the calculation of the amount of Restricted Payments;
- (4) so long as no Default has occurred and is continuing, the repurchase or other acquisition of shares of Capital Stock of the Company or any of its Subsidiaries from employees, former employees, directors or former directors of the Company or any of its Subsidiaries (or permitted transferees of such employees, former employees, directors or former directors), pursuant to the terms of the agreements (including employment agreements) or plans (or amendments thereto) approved by the Board of Directors under which such individuals purchase or sell or are granted the option to purchase or sell, shares of such Capital Stock; *provided, however*, that the aggregate amount of such repurchases and other acquisitions (excluding amounts representing cancellation of Indebtedness) shall not exceed US\$5 million in any calendar year; *provided further, however*, that such repurchases and other acquisitions shall be excluded in the calculation of the amount of Restricted Payments;
- (5) payments of dividends on Disqualified Stock issued pursuant to the covenant described under “—Limitation on Indebtedness”; *provided, however*, that such dividends shall be excluded in the calculation of the amount of Restricted Payments;
- (6) repurchases of Capital Stock deemed to occur upon exercise of stock options if such Capital Stock represents a portion of the exercise price of such options; *provided, however*, that such Restricted Payments shall be excluded in the calculation of the amount of Restricted Payments;
- (7) cash payments in lieu of the issuance of fractional shares in connection with the exercise of warrants, options or other securities convertible into or exchangeable for Capital Stock of the Company; *provided, however*, that any such cash payment shall not be for the purpose of evading the limitation of the covenant described under this subheading (as determined in good faith by the Board of Directors); *provided further, however*, that such payments shall be excluded in the calculation of the amount of Restricted Payments;
- (8) in the event of a Change of Control, and if no Default shall have occurred and be continuing, the payment, purchase, redemption, defeasance or other acquisition or retirement of Subordinated Obligations of the Company or any Subsidiary Guarantor, in each case, at a purchase price not greater than 101% of the principal amount of such Subordinated Obligations, plus any accrued and unpaid interest thereon; *provided, however*, that prior to such payment, purchase, redemption, defeasance or other acquisition or retirement, the Company (or a third party to the extent permitted by the Indenture) has made a Change of Control Offer with respect to the Notes as a result of such Change of Control and has repurchased all the Notes validly tendered and not withdrawn in connection with such Change of Control Offer; *provided further, however*, that such repurchase and other acquisitions shall be included in the calculation of the amount of Restricted Payments;

- (9) payments of intercompany subordinated Indebtedness, the Incurrence of which was permitted under clause (3) of paragraph (b) of the covenant described under “—Limitation on Indebtedness”; *provided, however*, that no Default has occurred and is continuing or would otherwise result therefrom; *provided further, however*, that such payments shall be excluded in the calculation of the amount of Restricted Payments; or
- (10) Restricted Payments in an amount which, when taken together with all Restricted Payments made pursuant to this clause (10), does not exceed US\$10 million; *provided, however*, that (A) at the time of each such Restricted Payment, no Default shall have occurred and be continuing (or result therefrom) and (B) such Restricted Payments shall be included in the calculation of the amount of Restricted Payments.

#### ***Limitation on Restrictions on Distributions from Restricted Subsidiaries***

The Company will not, and will not permit any Restricted Subsidiary to, create or otherwise cause or permit to exist or become effective any consensual encumbrance or restriction on the ability of any Restricted Subsidiary to (a) pay dividends or make any other distributions on its Capital Stock to the Company or a Restricted Subsidiary or pay any Indebtedness owed to the Company, (b) make any loans or advances to the Company or (c) transfer any of its property or assets to the Company, except:

- (1) with respect to clauses (a), (b) and (c),
  - (A) any encumbrance or restriction pursuant to an agreement in effect at or entered into on September 22, 2009;
  - (B) any encumbrance or restriction with respect to a Restricted Subsidiary pursuant to an agreement relating to any Indebtedness Incurred by such Restricted Subsidiary on or prior to the date on which such Restricted Subsidiary was acquired by the Company (other than Indebtedness Incurred as consideration in, or to provide all or any portion of the funds or credit support utilized to consummate, the transaction or series of related transactions pursuant to which such Restricted Subsidiary became a Restricted Subsidiary or was acquired by the Company) and outstanding on such date;
  - (C) any encumbrance or restriction pursuant to an agreement effecting a Refinancing of Indebtedness Incurred pursuant to an agreement referred to in clause (A) or (B) of clause (1) of this covenant or this clause (C) or contained in any amendment to an agreement referred to in clause (A) or (B) of clause (1) of this covenant or this clause (C); *provided, however*, that the encumbrances and restrictions with respect to such Restricted Subsidiary contained in any such refinancing agreement or amendment are no less favorable to the Noteholders than encumbrances and restrictions with respect to such Restricted Subsidiary contained in such predecessor agreements; and
  - (D) any encumbrance or restriction with respect to a Restricted Subsidiary imposed pursuant to an agreement entered into for the sale or disposition of all or substantially all the Capital Stock or assets of such Restricted Subsidiary pending the closing of such sale or disposition;
- (2) with respect to clause (c) only,
  - (A) any encumbrance or restriction consisting of customary non-assignment provisions in leases governing leasehold interests to the extent such provisions restrict the transfer of the lease or the property leased thereunder;
  - (B) any encumbrance or restriction contained in security agreements or mortgages securing Indebtedness of a Restricted Subsidiary to the extent such encumbrance or restriction restricts the transfer of the property subject to such security agreements or mortgages; and

- (C) customary provisions in partnership agreements, limited liability company organizational governance documents, joint venture agreements and other similar agreements entered into in the ordinary course of business that restrict the transfer of ownership interests in such partnership, limited liability company, joint venture or similar Person.

***Limitation on Sales of Assets and Subsidiary Stock***

(a) The Company will not, and will not permit any Restricted Subsidiary to, directly or indirectly, consummate any Asset Disposition unless:

- (1) the Company or such Restricted Subsidiary receives consideration at the time of such Asset Disposition at least equal to the fair market value (including as to the value of all non-cash consideration), as determined in good faith by the Board of Directors, of the shares and assets subject to such Asset Disposition;
- (2) except in the case of a Permitted Asset Swap, at least 75% of the consideration thereof received by the Company or such Restricted Subsidiary is in the form of cash or cash equivalents; and
- (3) an amount equal to 100% of the Net Available Cash from such Asset Disposition is applied by the Company (or such Restricted Subsidiary, as the case may be)
  - (A) *first*, to the extent the Company elects (or is required by the terms of any Indebtedness), (x) to prepay, repay, redeem, purchase, defease or otherwise acquire Senior Indebtedness of the Company or Indebtedness (other than any Disqualified Stock) of a Wholly Owned Subsidiary (in each case other than Indebtedness owed to the Company or an Affiliate of the Company) or (y) repay any Indebtedness that was secured by the assets sold in such Asset Disposition, in each case within one year from the later of the date of such Asset Disposition or the receipt of such Net Available Cash;
  - (B) *second*, to the extent of the balance of such Net Available Cash after application in accordance with clause (A), to the extent the Company elects, to acquire Additional Assets within one year from the later of the date of such Asset Disposition or the receipt of such Net Available Cash; and
  - (C) *third*, to the extent of the balance of such Net Available Cash after application in accordance with clauses (A) and (B), to make an offer to the Holders (and to holders of other Senior Indebtedness of the Company designated by the Company) to purchase Notes (and such other Senior Indebtedness of the Company) pursuant to and subject to the conditions contained in the Indenture;

*provided, however*, that in connection with any prepayment, repayment, purchase, redemption, defeasance or other acquisition of Indebtedness pursuant to clause (A) or (C) above, the Company or such Restricted Subsidiary shall permanently retire such Indebtedness and shall cause the related loan commitment (if any) to be permanently reduced in an amount equal to the principal amount so prepaid, repaid, purchased, redeemed, defeased or otherwise acquired.

Notwithstanding the foregoing provisions of this covenant, the Company and the Restricted Subsidiaries will not be required to apply any Net Available Cash in accordance with this covenant except to the extent that the aggregate Net Available Cash from all Asset Dispositions which is not applied in accordance with this covenant exceeds US\$10 million. Pending application of Net Available Cash pursuant to this covenant, such Net Available Cash shall be invested in Temporary Cash Investments or applied to temporarily reduce revolving credit indebtedness.

For the purposes of this covenant, the following are deemed to be cash or cash equivalents:

- (1) the assumption of Indebtedness of the Company (other than obligations in respect of Disqualified Stock of the Company) or any Restricted Subsidiary (other than obligations in respect of Disqualified Stock or Preferred Stock of a Subsidiary Guarantor) and the release of the Company or such Restricted Subsidiary from all liability on such Indebtedness in connection with such Asset Disposition; and
- (2) securities received by the Company or any Restricted Subsidiary from the transferee that are converted within 30 days by the Company or such Restricted Subsidiary into cash, to the extent of cash received in that conversion.

(b) In the event of an Asset Disposition that requires the purchase of the Notes (and other Senior Indebtedness of the Company) pursuant to clause (a)(3)(C) above, the Company will purchase New Notes tendered pursuant to an offer by the Company for the Notes (and such other Senior Indebtedness) at a purchase price of 100% of their principal amount (or, in the event such other Senior Indebtedness of the Company was issued with significant original issue discount, 100% of the accreted value thereof) without premium, plus accrued but unpaid interest (or, in respect of such other Senior Indebtedness of the Company, such lesser price, if any, as may be provided for by the terms of such Senior Indebtedness) in accordance with the procedures (including prorating in the event of oversubscription) set forth in the Indenture. If the aggregate purchase price of the securities tendered exceeds the Net Available Cash allotted to their purchase, the Company will select the securities to be purchased on a pro rata basis but in round denominations, which in the case of the Notes will be denominations of US\$1,000 principal amount or multiples thereof. The Company shall not be required to make such an offer to purchase the Notes (and other Senior Indebtedness of the Company) pursuant to this covenant if the Net Available Cash available therefor is less than US\$5 million (which lesser amount shall be carried forward for purposes of determining whether such an offer is required with respect to the Net Available Cash from any subsequent Asset Disposition). Upon completion of such an offer to purchase, Net Available Cash will be deemed to be reduced by the aggregate amount of such offer.

(c) The Company will comply, to the extent applicable, with the requirements of Section 14(e) of the Exchange Act and any other securities laws or regulations in connection with the repurchase of the Notes pursuant to this covenant. To the extent that the provisions of any securities laws or regulations conflict with provisions of this covenant, the Company will comply with the applicable securities laws and regulations and will not be deemed to have breached its obligations under this covenant by virtue of its compliance with such securities laws or regulations.

#### ***Limitation on Affiliate Transactions***

(a) The Company will not, and will not permit any Restricted Subsidiary to, enter into or permit to exist any transaction (including the purchase, sale, lease or exchange of any property, employee compensation arrangements or the rendering of any service) with, or for the benefit of, any Affiliate of the Company (an "Affiliate Transaction") unless:

- (1) the terms of the Affiliate Transaction are no less favorable to the Company or such Restricted Subsidiary than those that could be obtained at the time of the Affiliate Transaction in arm's-length dealings with a Person who is not an Affiliate;
- (2) if such Affiliate Transaction involves an amount in excess of US\$1 million, the terms of the Affiliate Transaction are set forth in writing and two Officers of the Company have certified that the criteria set forth in clause (1) are satisfied in an Officers' Certificate;
- (3) if such Affiliate Transaction involves an amount in excess of US\$5 million, a majority of the directors of the Company disinterested with respect to such Affiliate Transaction have determined in good faith that the criteria set forth in clause (1) are satisfied and have approved the relevant Affiliate Transaction as evidenced by a resolution of the Board of Directors; *provided, however*, that a director will not be

deemed disinterested with respect to transactions between the Company or a Restricted Subsidiary on the one hand and an immediate family member of such director or an entity affiliated with such immediate family member on the other hand; and

- (4) if such Affiliate Transaction involves an amount in excess of US\$25 million, the Board of Directors shall also have received a written opinion from an Independent Qualified Party to the effect that such Affiliate Transaction is fair, from a financial standpoint, to the Company and its Restricted Subsidiaries or is not less favorable to the Company and its Restricted Subsidiaries than could reasonably be expected to be obtained at the time in an arm's-length transaction with a Person who was not an Affiliate.
- (b) The provisions of the preceding paragraph (a) will not prohibit:
- (1) any Investment (other than a Permitted Investment) or other Restricted Payment, in each case permitted to be made pursuant to (but only to the extent included in the calculation of the amount of Restricted Payments made pursuant to paragraph (a) (3) of) the covenant described under “—Limitation on Restricted Payments”;
  - (2) any issuance of securities, or other payments, awards or grants in cash, securities or otherwise pursuant to, or the funding of, employment arrangements, stock options and stock ownership plans approved by the Board of Directors;
  - (3) loans or advances to employees in the ordinary course of business in accordance with the past practices of the Company or its Restricted Subsidiaries, but in any event not to exceed US\$2 million in the aggregate outstanding at any one time;
  - (4) the payment of reasonable fees to directors of the Company and its Restricted Subsidiaries who are not employees of the Company or its Restricted Subsidiaries;
  - (5) any transaction with a Subsidiary or joint venture or similar entity which would constitute an Affiliate Transaction solely because the Company or a Restricted Subsidiary owns an equity interest in or otherwise controls such Subsidiary, joint venture or similar entity;
  - (6) the issuance or sale of any Capital Stock (other than Disqualified Stock) of the Company; and
  - (7) transactions entered into in the ordinary course of business, consistent with past practices, on terms that are substantially similar to those that could be obtained at the time of such transactions in arm's-length dealings with a Person who is not an Affiliate.

#### ***Limitation on Line of Business***

The Company will not, and will not permit any Restricted Subsidiary, to engage in any business other than a Related Business.

#### ***Limitation on the Sale or Issuance of Capital Stock of Restricted Subsidiaries***

The Company

- (1) will not, and will not permit any Restricted Subsidiary to, sell, lease, transfer or otherwise dispose of any Capital Stock of any Restricted Subsidiary to any Person (other than the Company or a Wholly Owned Subsidiary), and
- (2) will not permit any Restricted Subsidiary to issue any of its Capital Stock (other than, if necessary, shares of its Capital Stock constituting directors' or other legally required qualifying shares) to any Person (other than to the Company or a Wholly Owned Subsidiary),



unless

- (A) immediately after giving effect to such issuance, sale or other disposition, neither the Company nor any of its Subsidiaries own any Capital Stock of such Restricted Subsidiary; or
- (B) immediately after giving effect to such issuance, sale or other disposition, such Restricted Subsidiary would no longer constitute a Restricted Subsidiary and any Investment in such Person remaining after giving effect thereto is treated as a new Investment by the Company and such Investment would be permitted to be made under the covenant described under “—Limitation on Restricted Payments” if made on the date of such issuance, sale or other disposition.

For purposes of this covenant, the creation of a Lien on any Capital Stock of a Restricted Subsidiary to secure Indebtedness of the Company or any of its Restricted Subsidiaries will not be deemed to be a violation of this covenant; *provided, however*, that any sale or other disposition by the secured party of such Capital Stock following foreclosure of its Lien will be subject to this covenant.

#### ***Limitation on Liens***

The Company will not, and will not permit any Restricted Subsidiary to, directly or indirectly, Incur or permit to exist any Lien (the “Initial Lien”) of any nature whatsoever on any of its properties (including Capital Stock of a Restricted Subsidiary), whether owned at September 22, 2009 or thereafter acquired, securing any Indebtedness, other than Permitted Liens, without effectively providing that the Notes shall be secured equally and ratably with (or prior to) the obligations so secured for so long as such obligations are so secured.

Any Lien created for the benefit of the Holders pursuant to the preceding sentence shall provide by its terms that such Lien shall be automatically and unconditionally released and discharged upon the release and discharge of the Initial Lien.

#### ***Limitation on Sale/Leaseback Transactions***

The Company will not, and will not permit any Restricted Subsidiary to, enter into any Sale/Leaseback Transaction with respect to any property unless:

- (1) the Company or such Restricted Subsidiary would be entitled to (A) Incur Indebtedness in an amount equal to the Attributable Debt with respect to such Sale/Leaseback Transaction pursuant to the covenant described under “—Limitation on Indebtedness” and (B) create a Lien on such property securing such Attributable Debt without equally and ratably securing the Notes pursuant to the covenant described under “—Limitation on Liens”;
- (2) the net proceeds received by the Company or any Restricted Subsidiary in connection with such Sale/Leaseback Transaction are at least equal to the fair market value (as determined by the Board of Directors) of such property; and
- (3) the Company applies the proceeds of such transaction in compliance with the covenant described under “—Limitation on Sale of Assets and Subsidiary Stock.”

#### ***Merger and Consolidation***

The Company will not consolidate with or merge with or into, or convey, transfer or lease, in one transaction or a series of transactions, directly or indirectly, all or substantially all its assets to, any Person, unless:

- (1) the resulting, surviving or transferee Person (the “Successor Company”) shall be a Person organized and existing under the laws of the United Mexican States or the laws of any political subdivision thereof, the laws of the United States of America, any State thereof or the District of Columbia, or the

European Union or any of its member nations and the Successor Company (if not the Company) shall expressly assume, by an indenture supplemental thereto, executed and delivered to the Trustee, in form satisfactory to the Trustee, all the obligations of the predecessor Company under the Notes and the Indenture;

- (2) immediately after giving *pro forma* effect to such transaction (and treating any Indebtedness which becomes an obligation of the Successor Company or any Subsidiary as a result of such transaction as having been Incurred by such Successor Company or such Subsidiary at the time of such transaction), no Default shall have occurred and be continuing;
- (3) immediately after giving *pro forma* effect to such transaction, the Successor Company would be able to Incur an additional US\$1.00 of Indebtedness pursuant to paragraph (a) of the covenant described under “—Limitation on Indebtedness”;
- (4) the Company shall have delivered to the Trustee an Officers’ Certificate and an Opinion of Counsel, each stating that such consolidation, merger or transfer and such supplemental indenture (if any) comply with the Indenture;
- (5) the Company shall have delivered to the Trustee an Opinion of Counsel to the effect that the Holders will not recognize income, gain or loss for U.S. Federal income tax purposes as a result of such transaction and will be subject to U.S. Federal income tax on the same amounts, in the same manner and at the same times as would have been the case if such transaction had not occurred; and
- (6) the Company shall have delivered an Opinion of Counsel in the United Mexican States to the effect that the Holders will not recognize income gain or loss for income tax purposes of such jurisdiction as a result of such transaction and will be subject to income tax in such jurisdiction on the same amounts, in the same manner and at the same times as would have been the case if such transaction had not occurred.

*provided, however*, that clause (3) will not be applicable to (A) a Restricted Subsidiary consolidating with, merging into or transferring all or part of its properties and assets to the Company or a Subsidiary Guarantor or (B) the Company merging with an Affiliate of the Company solely for the purpose and with the sole effect of reincorporating the Company in another jurisdiction.

For purposes of this covenant, the sale, lease, conveyance, assignment, transfer or other disposition of all or substantially all of the properties and assets of one or more Subsidiaries of the Company, which properties and assets, if held by the Company instead of such Subsidiaries, would constitute all or substantially all of the properties and assets of the Company on a consolidated basis, shall be deemed to be the transfer of all or substantially all of the properties and assets of the Company.

The Successor Company will be the successor to the Company and shall succeed to, and be substituted for, and may exercise every right and power of, the Company under the Indenture, and the predecessor Company, except in the case of a lease, shall be released from the obligation to pay the principal of and interest on the Notes.

The Company will not permit any Subsidiary Guarantor to consolidate with or merge with or into, or convey, transfer or lease, in one transaction or a series of transactions, all or substantially all of its assets to any Person unless:

- (1) except in the case of a Subsidiary Guarantor (x) that has been disposed of in its entirety to another Person (other than to the Company or an Affiliate of the Company), whether through a merger, consolidation or sale of Capital Stock or assets or (y) that, as a result of the disposition of all or a portion of its Capital Stock, ceases to be a Subsidiary, the resulting, surviving or transferee Person (if not such Subsidiary) shall be a Person organized and existing under the laws of the jurisdiction under which such Subsidiary was organized or under the laws of the United States of America, or any State

thereof or the District of Columbia or the United Mexican States, and such Person shall expressly assume, by a Guaranty Agreement, in a form satisfactory to the Trustee, all the obligations of such Subsidiary, if any, under its Subsidiary Guaranty;

- (2) immediately after giving effect to such transaction or transactions on a *pro forma* basis (and treating any Indebtedness which becomes an obligation of the resulting, surviving or transferee Person as a result of such transaction as having been issued by such Person at the time of such transaction), no Default shall have occurred and be continuing; and
- (3) the Company delivers to the Trustee an Officers' Certificate and an Opinion of Counsel, each stating that such consolidation, merger or transfer and such Guaranty Agreement, if any, complies with the Indenture.

### ***Future Guarantors***

The Company will cause each Restricted Subsidiary that Incurs any Indebtedness to, at the same time, execute and deliver to the Trustee a Guaranty Agreement pursuant to which such Restricted Subsidiary will Guarantee payment of the Notes on the same terms and conditions as those set forth in the Indenture.

### ***Reports to Holders***

The Company will provide to the Trustee and each Holder and make available to securities analysts and prospective investors the following information:

- (1) an English language translation of each report that the Company or any Restricted Subsidiary files with or provides to, or is required to file with or provide to, the Bolsa Mexicana de Valores or any other securities exchange on which securities of the Company or any Restricted Subsidiary are listed, promptly after such report is so filed or provided, which report shall be prepared in all material respects in accordance with all the rules and regulations applicable to such report and shall be filed or provided within the time periods required of such report; and
- (2) to the extent not included in the information required by clause (1) above:
  - (a) an English language version of the Company's annual audited consolidated financial statements, prepared in accordance with GAAP, promptly upon such financial statements becoming available but not later than 180 days after the end of the Company's relevant fiscal year, together with a "Management's Discussion and Analysis of Financial Condition and Results of Operations of Axtel" that includes at minimum (i) a discussion of the causes of material changes from year to year in line items in the Company's consolidated statement of operations, (ii) a description of the Company's material sources and uses of liquidity, (iii) a discussion of any material trends affecting the business, (iv) a discussion of any off-balance sheet arrangements and (v) a tabular disclosure of contractual obligations;
  - (b) an English language version of the Company's unaudited quarterly consolidated financial statements, prepared in accordance with GAAP, promptly upon such financial statements becoming available but not later than 60 days after the end of the Company's relevant fiscal quarter, together with a "Management's Discussion and Analysis of Financial Condition and Results of Operations of Axtel" that includes at minimum (i) a discussion of the causes of material changes in the current fiscal year to date from the same period in the prior fiscal year in line items in the Company's consolidated statement of operations, (ii) a description of the Company's material sources and uses of liquidity, (iii) a discussion of any material trends affecting the business and (iv) a discussion of any off-balance sheet arrangements;
  - (c) at any time that any of the Company's Subsidiaries are not Subsidiary Guarantors, then the financial statements described in clauses (a) and (b) will include, in a footnote, condensed consolidating financial information for the same periods with a separate column for: (i) the

Company, (ii) the Subsidiary Guarantors on a combined basis, (iii) all Subsidiaries that are not Subsidiary Guarantors on a combined basis, (iv) consolidating adjustments and (v) the total consolidated amounts; *provided, however*, that at least one of the total assets, revenues, income from continuing operations before income taxes, and cash flow from operating activities of the Subsidiaries that are not Subsidiary Guarantors on a combined basis is at least 3% of the corresponding amount for the Company and its Subsidiaries on a consolidated basis;

- (d) at any time that any of the Company's Subsidiaries are Unrestricted Subsidiaries, the financial statements described in clauses (a) and (b) will be accompanied by internally prepared reconciliations or adjustments to the financial information of the Company and its Subsidiaries sufficient to demonstrate compliance with the covenants set forth in the Indenture;
- (e) a brief description of any transaction or series of similar transactions to which the Company or any of its Subsidiaries is a party and in which any of the following persons has or will have a direct or indirect material interest: (1) any director or officer of the Company, (2) any nominee for election as a director, (3) any Affiliate of the Company, and (4) any member of the immediate family of any of the foregoing; and
- (f) so long as the Notes are not freely transferable under the Securities Act, any information required to be delivered pursuant to Rule 144A(d)(4) under the Securities Act.

The Company will be deemed to have provided such information to Holders, securities analysts and prospective investors by (a) including such information in documents filed with or furnished to the SEC for public availability or (b) posting reports including such information on its website, each within the time periods specified above. Delivery of such reports, information and documents to the Trustee shall be for informational purposes only and the Trustee's receipt of such shall not constitute constructive notice of any information contained therein or determinable from information contained therein, including our compliance with any of the covenants contained in the Indenture (as to which the Trustee will be entitled to conclusively rely upon an Officer's Certificate.)

## Defaults

Each of the following is an "Event of Default":

- (1) a default in the payment of interest on the Notes when due, continued for 30 days;
- (2) a default in the payment of principal of any Note when due at its Stated Maturity, upon optional redemption, upon required purchase, upon declaration of acceleration or otherwise;
- (3) the failure by the Company to comply with its obligations under "—Certain Covenants—Merger and Consolidation" above;
- (4) the failure by the Company to comply for 30 days after notice with any of its obligations in the covenants described above under "Change of Control" (other than a failure to purchase Notes) or under "—Certain Covenants" under "—Limitation on Indebtedness," "—Limitation on Restricted Payments," "—Limitation on Restrictions on Distributions from Restricted Subsidiaries," "—Limitation on Sales of Assets and Subsidiary Stock" (other than a failure to purchase Notes), "—Limitation on Affiliate Transactions," "—Limitation on Line of Business," "—Limitation on the Sale or Issuance of Capital Stock of Restricted Subsidiaries," or "—Limitation on Liens," "—Limitation on Sale/Leaseback Transactions," "—Future Guarantors," or "—Reports to Holders";
- (5) the failure by the Company or any Subsidiary Guarantor to comply for 60 days after notice with its other agreements contained in the Indenture;
- (6) Indebtedness of the Company, any Subsidiary Guarantor or any Significant Subsidiary is not paid within any applicable grace period after final maturity or is accelerated by the Holders thereof because of a default and the total amount of such Indebtedness unpaid or accelerated exceeds US\$20 million (the "cross acceleration provision");

- (7) certain events of bankruptcy, concurso mercantil, quiebra, insolvency or reorganization of the Company, a Subsidiary Guarantor or any Significant Subsidiary (the “bankruptcy provisions”);
- (8) any judgment or decree for the payment of money in excess of US\$20 million is entered against the Company, a Subsidiary Guarantor or any Significant Subsidiary, remains outstanding for a period of 60 consecutive days following such judgment and is not discharged, waived or stayed (the “judgment default provision”); or
- (9) a Subsidiary Guaranty ceases to be in full force and effect (other than in accordance with the terms of such Subsidiary Guaranty) or a Subsidiary Guarantor denies or disaffirms its obligations under its Subsidiary Guaranty.

However, a default under clauses (4) and (5) will not constitute an Event of Default until the Trustee or the Holders of 25% in principal amount of the outstanding Notes notify the Company of the default and the Company does not cure such default within the time specified after receipt of such notice.

If an Event of Default occurs and is continuing, the Trustee or the Holders of at least 25% in principal amount of the outstanding Notes may declare the principal of and accrued but unpaid interest on all the Notes to be due and payable. Upon such a declaration, such principal and interest shall be due and payable immediately. If an Event of Default relating to certain events of bankruptcy, insolvency or reorganization of the Company occurs and is continuing, the principal of and interest on all the Notes will ipso facto become and be immediately due and payable without any declaration or other act on the part of the Trustee or any Holders. Under certain circumstances, the Holders of a majority in principal amount of the outstanding Notes may rescind any such acceleration with respect to the Notes and its consequences, *provided* that there had been paid or deposited with the Trustee a sum sufficient to pay all amounts due to the Trustee and to reimburse the Trustee for any and all fees, expenses and disbursements advanced by the Trustee, its agents and its counsel incurred in connection with such Default.

Subject to the provisions of the Indenture relating to the duties of the Trustee, in case an Event of Default occurs and is continuing, the Trustee will be under no obligation to exercise any of the rights or powers under the Indenture at the request or direction of any of the Holders unless such Holders have offered to the Trustee indemnity satisfactory to it or security against any loss, liability or expense. Except to enforce the right to receive payment of principal, premium (if any) or interest when due, no Holder may pursue any remedy with respect to the Indenture or the Notes unless:

- (1) such Holder has previously given the Trustee notice that an Event of Default is continuing;
- (2) Holders of at least 25% in principal amount of the outstanding Notes have requested the Trustee to pursue the remedy;
- (3) such Holders have offered the Trustee security or indemnity satisfactory to it against any loss, liability or expense;
- (4) the Trustee has not complied with such request within 60 days after the receipt thereof and the offer of security or indemnity; and
- (5) Holders of a majority in principal amount of the outstanding Notes have not given the Trustee a direction inconsistent with such request within such 60-day period.

Subject to certain restrictions set forth in the Indenture, the Holders of a majority in principal amount of the outstanding Notes are given the right to direct the time, method and place of conducting any proceeding for any remedy available to the Trustee or of exercising any trust or power conferred on the Trustee. The Trustee, however, may refuse to follow any direction that conflicts with law or the Indenture or that the Trustee determines is unduly prejudicial to the rights of any other Holder or that would involve the Trustee in personal liability.

If a Default occurs, is continuing and is known to the Trustee, the Trustee must mail to each Holder notice of the Default within 90 days after it occurs. Except in the case of a Default in the payment of principal of or interest on any Note, the Trustee may withhold notice if and so long as a committee of its Trust Officers determines that withholding notice is not opposed to the interest of the Holders. In addition, we are required to deliver to the Trustee, within 120 days after the end of each fiscal year, a certificate indicating whether the signers thereof know of any Default that occurred during the previous year. We are required to deliver to the Trustee, within 30 days after the occurrence thereof, written notice of any event which would constitute certain Defaults, their status and what action we are taking or propose to take in respect thereof.

### **Amendments and Waivers**

Subject to certain exceptions, the Indenture may be amended with the consent of the Holders of a majority in principal amount of the Notes then outstanding (including consents obtained in connection with a tender offer or exchange for the Notes) and any past default or compliance with any provisions may also be waived with the consent of the Holders of a majority in principal amount of the Notes then outstanding. However, without the consent of each Holder of an outstanding Note affected thereby, an amendment or waiver may not, among other things:

- (1) reduce the amount of the Notes whose Holders must consent to an amendment;
- (2) reduce the rate of or extend the time for payment of interest on any Note;
- (3) reduce the principal of or change the Stated Maturity of any Note;
- (4) change the provisions of the Indenture applicable to the redemption of any Note;
- (5) make any Note payable in money other than that stated in the Note;
- (6) impair the right of any Holder to receive payment of principal of and interest on such Holder's Notes on or after the due dates therefor or to institute suit for the enforcement of any payment on or with respect to such Holder's Notes;
- (7) make any change in, the amendment provisions which require each Holder's consent or in the waiver provisions;
- (8) make any change in the ranking or priority of any Note that would adversely affect the Noteholders;
- (9) make any change in, or release other than in accordance with the Indenture, any Subsidiary Guaranty that would adversely affect the Noteholders; or
- (10) make any change in the provisions of the Indenture described under "—Additional Amounts" that adversely affects the rights of any Noteholder or amend the terms of the Notes or the Indenture in any way that would result in the loss of an exemption from any of the Taxes described thereunder.

Notwithstanding the preceding, without the consent of any Holder, the Company, the Subsidiary Guarantors and Trustee may amend the Indenture:

- (1) to cure any ambiguity, omission, defect or inconsistency;
- (2) to provide for the assumption by a successor corporation of the obligations of the Company, or any Subsidiary Guarantor under the Indenture;
- (3) to provide for uncertificated Notes in addition to or in place of certificated Notes (*provided* that the uncertificated Notes are issued in registered form for purposes of Section 163(f) of the Code, or in a manner such that the uncertificated Notes are described in Section 163(f)(2)(B) of the Code);
- (4) to add Guarantees with respect to the Notes, including any Subsidiary Guaranties, or to secure the Notes;



- (5) to add to the covenants of the Company or a Subsidiary Guarantor for the benefit of the Holders or to surrender any right or power conferred upon the Company or a Subsidiary Guarantor;
- (6) to make any change that does not adversely affect the rights of any Holder; or
- (7) to make any amendment to the provisions of the Indenture relating to the form, authentication, transfer and legending of Notes; *provided, however*, that (a) compliance with the Indenture as so amended would not result in Notes being transferred in violation of the Securities Act or any other applicable securities law and (b) such amendment does not materially affect the rights of Holders to transfer Notes.

The consent of the Holders is not necessary under the Indenture to approve the particular form of any proposed amendment. It is sufficient if such consent approves the substance of the proposed amendment.

After an amendment under the Indenture becomes effective, we are required to mail to Holders a notice briefly describing such amendment. However, the failure to give such notice to all Holders, or any defect therein, will not impair or affect the validity of the amendment.

### **Transfer**

The Notes will be issued in registered form and will be transferable only upon the surrender of the Notes being transferred for registration of transfer. We may require payment of a sum sufficient to cover any tax, assessment or other governmental charge payable in connection with certain transfers and exchanges.

### **Defeasance**

At any time, we may terminate all our obligations under the Notes and the Indenture (“legal defeasance”), except for certain obligations, including those respecting the defeasance trust and obligations to register the transfer or exchange of the Notes, to replace mutilated, destroyed, lost or stolen Notes and to maintain a registrar and paying agent in respect of the Notes.

In addition, at any time we may terminate our obligations under “—Change of Control” and under the covenants described under “—Certain Covenants” (other than the covenant described under “—Merger and Consolidation”), the operation of the cross acceleration provision, the bankruptcy provisions with respect to Subsidiary Guarantors and Significant Subsidiaries and the judgment default provision described under “—Defaults” above and the limitations contained in clause (3) of the first paragraph under “—Certain Covenants—Merger and Consolidation” above (“covenant defeasance”).

We may exercise our legal defeasance option notwithstanding our prior exercise of our covenant defeasance option. If we exercise our legal defeasance option, payment of the Notes may not be accelerated because of an Event of Default with respect thereto. If we exercise our covenant defeasance option, payment of the Notes may not be accelerated because of an Event of Default specified in clause (4), (6), (7) (with respect only to Significant Subsidiaries and Subsidiary Guarantors) or (8) under “—Defaults” above or because of the failure of the Company to comply with clause (3) of the first paragraph under “—Certain Covenants—Merger and Consolidation” above. If we exercise our legal defeasance option or our covenant defeasance option, each Subsidiary Guarantor will be released from all of its obligations with respect to the its Subsidiary Guaranty.

In order to exercise either of our defeasance options, we must irrevocably deposit in trust (the “defeasance trust”) with the Trustee money or U.S. Government Obligations for the payment of principal and interest on the Notes to redemption or maturity, as the case may be, and must comply with certain other conditions, including delivery to the Trustee of (1) an Opinion of Counsel to the effect that Holders will not recognize income, gain or loss for U.S. Federal income tax purposes as a result of such deposit and defeasance and will be subject to U.S. Federal income tax on the same amounts and in the same manner and at the same times as would have been the

case if such deposit and defeasance had not occurred (and, in the case of legal defeasance only, such Opinion of Counsel must be based on a ruling of the Internal Revenue Service or other change in applicable U.S. Federal income tax law) and (2) an Opinion of Counsel in the United Mexican States to the effect that Holders will not recognize income, gain or loss for income tax purposes of such jurisdiction as a result of such deposit and defeasance and will be subject to income tax of such jurisdiction on the same amounts and in the same manner and at the same times as would have been the case if such deposit and defeasance had not occurred.

### **Concerning the Trustee**

The Bank of New York Mellon is to be the Trustee under the Indenture. We have appointed The Bank of New York Mellon as registrar (the “Registrar”) and paying agent with regard to the Notes.

The Indenture contains certain limitations on the rights of the Trustee, should it become a creditor of the Company or any Subsidiary Guarantor, to obtain payment of claims in certain cases, or to realize on certain property received in respect of any such claim as security or otherwise. The Trustee will be permitted to engage in other transactions; *provided, however*, if it acquires any conflicting interest it must either eliminate such conflict within 90 days or resign.

The Holders of a majority in principal amount of the outstanding Notes will have the right to direct the time, method and place of conducting any proceeding for exercising any remedy available to the Trustee, subject to certain exceptions. If an Event of Default occurs (and is not cured), the Trustee will be required, in the exercise of its power, to use the degree of care of a prudent man in the conduct of his own affairs. Subject to such provisions, the Trustee will be under no obligation to exercise any of its rights or powers under the Indenture at the request of any Holder, unless such Holder shall have offered to the Trustee security and indemnity satisfactory to it against any loss, liability or expense and then only to the extent required by the terms of the Indenture.

### **No Personal Liability of Directors, Officers, Employees and Stockholders**

No director, officer, employee, incorporator or stockholder of the Company or any Subsidiary Guarantor will have any liability for any obligations of the Company or any Subsidiary Guarantor under the Notes, any Subsidiary Guaranty or the Indenture or for any claim based on, in respect of, or by reason of such obligations or their creation. Each Holder by accepting a Note waives and releases all such liability. The waiver and release are part of the consideration for issuance of the Notes. Such waiver and release may not be effective to waive liabilities under the U.S. Federal securities laws, and it is the view of the SEC that such a waiver is against public policy.

### **Governing Law**

The Indenture and the Notes will be governed by, and construed in accordance with, the laws of the State of New York.

### **Enforceability of Judgments**

Since all of our operating assets and the operating assets of our subsidiaries are situated outside the United States, any judgment obtained in the United States against us or our subsidiaries, including judgments with respect to the payment of principal, interest, redemption price and any purchase price with respect to the Notes, may not be collectible within the United States.

A judgment obtained in a competent State or Federal court sitting in the Borough of Manhattan, City of New York, United States of America arising out of or in relation to the obligations of the Company under the Notes would be enforceable in Mexico against us or our subsidiaries, *provided* that all federal and state procedural

requirements under Mexican law (as the applicable case may be), including laws concerning statute of limitations and expirations, are satisfied; and further *provided* that, among others:

- (1) such judgment is final in the rendering state and obtained in compliance with legal requirements of the jurisdiction of the court rendering such judgment and such judgment is in compliance with the terms set forth in the Notes and all legal requirements as the case may be;
- (2) such judgment is strictly for the payment of a certain sum of money, based on an *in personam* action (*acción personal*) as opposed to an *in rem* action (*acción real*);
- (3) the judge or court rendering the judgment is considered to have jurisdiction and is competent to hear and judge on the subject matter of the case in accordance with accepted principals of international law that are compatible and analogous with Mexican laws, and the subject matter of the case was not of the exclusive jurisdiction of Mexican courts;
- (4) service of process in the action has been served personally on the defendant or on a duly appointed process agent;
- (5) such judgment does not contravene Mexican law, public policy of Mexico, international treaties or agreements binding upon Mexico or generally accepted principles of international law;
- (6) the applicable procedure under the laws of México with respect to the enforcement of foreign judgments (including issuance of a *rogatory letter (carta rogatoria)* by the competent authority of such jurisdiction requesting enforcement of such judgment and the certification of such judgment as authentic by the corresponding authorities of such jurisdiction in accordance with the laws thereof) is complied with;
- (7) the courts of such jurisdiction would enforce Mexican judgments as a matter of reciprocity;
- (8) the action in respect of which such judgment is rendered is not the subject matter of a lawsuit or legal proceedings among the same parties that is or are pending before a Mexican court, or was resolved by or conflicts with a definitive judgment previously rendered by a Mexican court that has previously served process or delivered a rogatory letter (*carta rogatoria*) to the competent authorities in accordance with the Mexican law;
- (9) the court that rendered such judgment has jurisdiction over the debtor as recognized by the courts of Mexico and in accordance with its conflict of laws rules; and
- (10) the judgment fulfills all necessary requirements to be considered authentic.

### **Consent to Jurisdiction and Service**

The Company, each Subsidiary Guarantor and the Trustee consent that any legal action, suit or proceeding arising out of or relating to the Notes may be instituted in the United States District Court of the Southern District of New York and the courts of the State of New York sitting in New York, Borough of Manhattan, and will submit to and accept the jurisdiction of any such court.

The Company and each Subsidiary Guarantor will irrevocably appoint CT Corporation System, domiciled at 111 Eighth Avenue, New York, New York 10011 as its agent for service of process for actions relating to the Notes, the Purchase Agreement or the Indenture brought under Federal or state securities laws brought in the United States District Court of the Southern District of New York and the courts of the State of New York sitting in New York, Borough of Manhattan. For such purposes, the Company and each Subsidiary Guarantor will grant to CT Corporation System a special, irrevocable power of attorney for lawsuits and collections (*pleitos y cobranzas*) in the presence of a Mexican Notary Public, in form and substance satisfactory to the Trustee.

## Certain Definitions

“*Additional Assets*” means:

- (1) any property, plant, equipment or licenses used in a Related Business;
- (2) the Capital Stock of a Person that becomes a Restricted Subsidiary as a result of the acquisition of such Capital Stock by the Company or another Restricted Subsidiary; or
- (3) Capital Stock constituting a minority interest in any Person that at such time is a Restricted Subsidiary;

*provided, however*, that any such Restricted Subsidiary described in clause (2) or (3) above is primarily engaged in a Related Business.

“*Adjusted Consolidated Net Income*” for any period means Consolidated Net Income

- (1) plus, to the extent deducted in calculating such Consolidated Net Income, depreciation and amortization expense of the Company and its consolidated Restricted Subsidiaries (excluding amortization expense attributable to a prepaid operating activity item that was paid in cash in a prior period) for such period;
- (2) less capital expenditures made by the Company and its Restricted Subsidiaries for such period.

“*Affiliate*” of any specified Person means any other Person, directly or indirectly, controlling or controlled by or under direct or indirect common control with such specified Person. For the purposes of this definition, “control” when used with respect to any Person means the power to direct the management and policies of such Person, directly or indirectly, whether through the ownership of voting securities, by contract or otherwise; and the terms “controlling” and “controlled” have meanings correlative to the foregoing. For purposes of the covenants described under “—Certain Covenants—Limitation on Restricted Payments,” “—Certain Covenants—Limitation on Affiliate Transactions” and “—Certain Covenants—Limitation on Sales of Assets and Subsidiary Stock” only, “Affiliate” shall also mean any beneficial owner of Capital Stock representing 15% or more of the total voting power of the Voting Stock (on a fully diluted basis) of the Company or of rights or warrants to purchase such Capital Stock (whether or not currently exercisable) and any Person who would be an Affiliate of any such beneficial owner pursuant to the first sentence hereof.

“*Asset Disposition*” means any sale, lease, transfer or other disposition (or series of related sales, leases, transfers or dispositions) by the Company or any Restricted Subsidiary, including any disposition by means of a merger, consolidation or similar transaction (each referred to for the purposes of this definition as a “disposition”), of:

- (1) any shares of Capital Stock of a Restricted Subsidiary (other than directors’ qualifying shares or shares required by applicable law to be held by a Person other than the Company or a Restricted Subsidiary);
- (2) all or substantially all the assets of any division or line of business of the Company or any Restricted Subsidiary; or
- (3) any other assets of the Company or any Restricted Subsidiary outside of the ordinary course of business of the Company or such Restricted Subsidiary (other than, in the case of clauses (1), (2) and (3) above,
  - (A) a disposition by a Restricted Subsidiary to the Company or by the Company or a Restricted Subsidiary to a Wholly Owned Subsidiary;
  - (B) for purposes of the covenant described under “—Certain Covenants—Limitation on Sales of Assets and Subsidiary Stock” only, (i) a disposition that constitutes a Restricted Payment (or would constitute a Restricted Payment but for the exclusions from the definition thereof) and that is not prohibited by the covenant described under “—Certain Covenants—Limitation on Restricted Payments” and (ii) a disposition of all or substantially all the assets of the Company in accordance with the covenant described under “—Certain Covenants—Merger and Consolidation”;

- (C) a disposition of assets with a fair market value of less than US\$1,000,000;
- (D) a disposition of cash or Temporary Cash Investments; and
- (E) the creation of a Lien (but not the sale or other disposition of the property subject to such Lien)).

“*Attributable Debt*” in respect of a Sale/Leaseback Transaction means, as at the time of determination, the present value (discounted at the interest rate borne by the Notes, compounded annually) of the total obligations of the lessee for rental payments during the remaining term of the lease included in such Sale/Leaseback Transaction (including any period for which such lease has been extended); *provided, however*, that if such Sale/Leaseback Transaction results in a Capital Lease Obligation, the amount of Indebtedness represented thereby will be determined in accordance with the definition of “Capital Lease Obligation.”

“*Avantel/Telmex IRU*” means the indefeasible right to use certain telecommunications capacity pursuant to an agreement between the Company and Telmex originally entered into on January 2, 2006.

“*Average Life*” means, as of the date of determination, with respect to any Indebtedness, the quotient obtained by dividing:

- (1) the sum of the products of the numbers of years from the date of determination to the dates of each successive scheduled principal payment of or redemption or similar payment with respect to such Indebtedness multiplied by the amount of such payment by
- (2) the sum of all such payments.

“*Board of Directors*” means the Board of Directors of the Company or any committee thereof duly authorized to act on behalf of such Board of Directors.

“*Business Day*” means each day which is not a Legal Holiday.

“*Capital Lease Obligation*” means an obligation that is required to be classified and accounted for as a capital lease for financial reporting purposes in accordance with GAAP, and the amount of Indebtedness represented by such obligation shall be the capitalized amount of such obligation determined in accordance with GAAP; and the Stated Maturity thereof shall be the date of the last payment of rent or any other amount due under such lease prior to the first date upon which such lease may be terminated by the lessee without payment of a penalty. For purposes of the covenant described under “—Certain Covenants—Limitations on Liens,” a Capital Lease Obligation will be deemed to be secured by a Lien on the property being leased.

“*Capital Stock*” of any Person means any and all shares, interests (including partnership interests), rights to purchase, warrants, options, participations or other equivalents of or interests in (however designated) equity of such Person, including any Preferred Stock, but excluding any debt securities convertible into such equity.

“*Code*” means the Internal Revenue Code of 1986, as amended.

“*Consolidated Interest Expense*” means, for any period, the total interest expense of the Company and its consolidated Restricted Subsidiaries.

“*Consolidated Leverage Ratio*” as of any date of determination means the ratio of (a) the aggregate amount of Indebtedness of the Company and its Restricted Subsidiaries as of such date of determination to (b) EBITDA for the most recent four consecutive fiscal quarters ending at least 45 days prior to such date of determination (the “Reference Period”); *provided, however*, that:

- (1) if the transaction giving rise to the need to calculate the Consolidated Leverage Ratio is an Incurrence of Indebtedness, the amount of such Indebtedness shall be calculated after giving effect on a *pro forma* basis to such Indebtedness;

- (2) if the Company or any Restricted Subsidiary has repaid, repurchased, defeased or otherwise discharged any Indebtedness that was outstanding as of the end of such fiscal quarter or if any Indebtedness is to be repaid, repurchased, defeased or otherwise discharged on the date of the transaction giving rise to the need to calculate the Consolidated Leverage Ratio (other than, in each case, Indebtedness Incurred under any revolving credit agreement), the aggregate amount of Indebtedness shall be calculated on a *pro forma* basis and EBITDA shall be calculated as if the Company or such Restricted Subsidiary had not earned the interest income, if any, actually earned during the Reference Period in respect of cash or Temporary Cash Investments used to repay, repurchase, defease or otherwise discharge such Indebtedness;
- (3) if since the beginning of the Reference Period the Company or any Restricted Subsidiary shall have made any Asset Disposition, the EBITDA for the Reference Period shall be reduced by an amount equal to the EBITDA (if positive) directly attributable to the assets which are the subject of such Asset Disposition for the Reference Period or increased by an amount equal to the EBITDA (if negative) directly attributable thereto for the Reference Period;
- (4) if since the beginning of the Reference Period the Company or any Restricted Subsidiary (by merger or otherwise) shall have made an Investment in any Restricted Subsidiary (or any Person which becomes a Restricted Subsidiary) or an acquisition of assets which constitutes all or substantially all of an operating unit of a business, EBITDA for the Reference Period shall be calculated after giving *pro forma* effect thereto (including the Incurrence of any Indebtedness) as if such Investment or acquisition occurred on the first day of the Reference Period; and
- (5) if since the beginning of the Reference Period any Person (that subsequently became a Restricted Subsidiary or was merged with or into the Company or any Restricted Subsidiary since the beginning of such Reference Period) shall have made any Asset Disposition, any Investment or acquisition of assets that would have required an adjustment pursuant to clause (3) or (4) above if made by the Company or a Restricted Subsidiary during the Reference Period, EBITDA for the Reference Period shall be calculated after giving *pro forma* effect thereto as if such Asset Disposition, Investment or acquisition occurred on the first day of the Reference Period.

For purposes of this definition, whenever *pro forma* effect is to be given to an acquisition of assets, the amount of income or earnings relating thereto and the amount of Consolidated Interest Expense associated with any Indebtedness Incurred in connection therewith, the *pro forma* calculations shall be determined in good faith by a responsible financial or accounting Officer of the Company. If any Indebtedness bears a floating rate of interest and is being given *pro forma* effect, the interest on such Indebtedness shall be calculated as if the rate in effect on the date of determination had been the applicable rate for the entire period (taking into account any Interest Rate Agreement applicable to such Indebtedness if such Interest Rate Agreement has a remaining term in excess of 12 months).

If any Indebtedness is Incurred under a revolving credit facility and is being given *pro forma* effect, the interest on such Indebtedness shall be calculated based on the average daily balance of such Indebtedness for the four fiscal quarters subject to the *pro forma* calculation to the extent that such Indebtedness was incurred solely for working capital purposes.

“*Consolidated Net Income*” means, for any period, the net income of the Company and its consolidated Subsidiaries; *provided, however*, that there shall not be included in such Consolidated Net Income:

- (1) any net income of any Person (other than the Company) if such Person is not a Restricted Subsidiary, except that:
  - (A) subject to the exclusion contained in clause (4) below, the Company’s equity in the net income of any such Person for such period shall be included in such Consolidated Net Income up to the aggregate amount of cash actually distributed by such Person during such period to the Company



or a Restricted Subsidiary as a dividend or other distribution (subject, in the case of a dividend or other distribution paid to a Restricted Subsidiary, to the limitations contained in clause (3) below); and

- (B) the Company's equity in a net loss of any such Person for such period shall be included in determining such Consolidated Net Income;
- (2) any net income (or loss) of any Person acquired by the Company or a Subsidiary in a pooling of interests transaction (or any transaction accounted for in a manner similar to a pooling of interests) for any period prior to the date of such acquisition;
- (3) any net income of any Restricted Subsidiary if such Restricted Subsidiary is subject to restrictions, directly or indirectly, on the payment of dividends or the making of distributions by such Restricted Subsidiary, directly or indirectly, to the Company, except that:
  - (A) subject to the exclusion contained in clause (4) below, the Company's equity in the net income of any such Restricted Subsidiary for such period shall be included in such Consolidated Net Income up to the aggregate amount of cash actually distributed by such Restricted Subsidiary during such period to the Company or another Restricted Subsidiary as a dividend or other distribution (subject, in the case of a dividend or other distribution paid to another Restricted Subsidiary, to the limitation contained in this clause); and
  - (B) the Company's equity in a net loss of any such Restricted Subsidiary for such period shall be included in determining such Consolidated Net Income;
- (4) any gain (or loss) realized upon the sale or other disposition of any assets of the Company, its consolidated Subsidiaries or any other Person (including pursuant to any sale-and-leaseback arrangement) which is not sold or otherwise disposed of in the ordinary course of business and any gain (or loss) realized upon the sale or other disposition of any Capital Stock of any Person;
- (5) any net, after-tax, extraordinary or non-recurring gains or losses or income or expenses; and
- (6) the cumulative effect of a change in accounting principles;

in each case, for such period. Notwithstanding the foregoing, for the purposes of the covenant described under “—Certain Covenants—Limitation on Restricted Payments” only, there shall be excluded from Consolidated Net Income any repurchases, repayments or redemptions of Investments, proceeds realized on the sale of Investments or return of capital to the Company or a Restricted Subsidiary to the extent such repurchases, repayments, redemptions, proceeds or returns increase the amount of Restricted Payments permitted under such covenant pursuant to clause (a)(3)(D) thereof.

“*Consolidated Net Tangible Assets*” means, as of any date of determination, the total assets shown on the consolidated balance sheet of the Company and its Restricted Subsidiaries as of the most recent date for which such a balance sheet is available, determined on a consolidated basis in accordance with GAAP, less all goodwill, patents, tradenames, trademarks, copyrights, franchises, experimental expenses, organization expenses and any other amounts classified as intangible assets in accordance with GAAP (and, in the case of any determination relating to any Investment, on a *pro forma* basis including any property or assets being acquired in connection therewith).

“*Consolidated Secured Leverage Ratio*” means, as of any date of determination, the ratio of (1) the aggregate amount of Indebtedness of the Company and its Restricted Subsidiaries that is secured by Liens as of such date of determination to (2) EBITDA for the period of (i) the most recent four consecutive fiscal quarters ending at least 45 days prior to the date of determination or (ii) if quarterly information is available for the immediately preceding fiscal quarter and such financial information is included in the reports filed or delivered pursuant to the covenant described under “Certain Covenants—SEC Reports,” the most recent four consecutive fiscal quarters, with such *pro forma* and other adjustments to each of Indebtedness and EBITDA as are appropriate and consistent with the *pro forma* and other adjustment provisions set forth in the definition of Consolidated Leverage Ratio.

“*Consolidated Total Assets*” means, as of any date of determination, the total assets shown on the consolidated balance sheet of the Company and its Restricted Subsidiaries as of the most recent date for which such a balance sheet is available, determined on a consolidated basis in accordance with GAAP (and, in the case of any determination relating to any Incurrence of Indebtedness or any Investment, on a *pro forma* basis including any property or assets being acquired in connection therewith).

“*Currency Agreement*” means any foreign exchange contract, currency swap agreement or other similar agreement with respect to currency values.

“*Default*” means any event which is, or after notice or passage of time or both would be, an Event of Default.

“*Disqualified Stock*” means, with respect to any Person, any Capital Stock which by its terms (or by the terms of any security into which it is convertible or for which it is exchangeable at the option of the holder) or upon the happening of any event:

- (1) matures or is mandatorily redeemable (other than redeemable only for Capital Stock of such Person which is not itself Disqualified Stock) pursuant to a sinking fund obligation or otherwise;
- (2) is convertible or exchangeable at the option of the holder for Indebtedness or Disqualified Stock; or
- (3) is mandatorily redeemable or must be purchased upon the occurrence of certain events or otherwise, in whole or in part;

in each case on or prior to the first anniversary of the Stated Maturity of the Notes; *provided, however*, that any Capital Stock that would not constitute Disqualified Stock but for provisions thereof giving holders thereof the right to require such Person to purchase or redeem such Capital Stock upon the occurrence of an “asset sale” or “change of control” occurring prior to the first anniversary of the Stated Maturity of the Notes shall not constitute Disqualified Stock if:

- (a) the “asset sale” or “change of control” provisions applicable to such Capital Stock are not more favorable to the holders of such Capital Stock than the terms applicable to the Notes and described under “—Certain Covenants—Limitation on Sales of Assets and Subsidiary Stock” and “—Certain Covenants—Change of Control”; and
- (b) any such requirement only becomes operative after compliance with such terms applicable to the Notes, including the purchase of any Notes tendered pursuant thereto.

The amount of any Disqualified Stock that does not have a fixed redemption, repayment or repurchase price will be calculated in accordance with the terms of such Disqualified Stock as if such Disqualified Stock were redeemed, repaid or repurchased on any date on which the amount of such Disqualified Stock is to be determined pursuant to the Indenture; *provided, however*, that if such Disqualified Stock could not be required to be redeemed, repaid or repurchased at the time of such determination, the redemption, repayment or repurchase price will be the book value of such Disqualified Stock as reflected in the most recent financial statements of such Person.

“*EBITDA*” for any period means the sum of Consolidated Net Income, plus the following to the extent deducted in calculating such Consolidated Net Income:

- (1) all expense for income tax or asset tax of the Company and its consolidated Restricted Subsidiaries;
- (2) Consolidated Interest Expense;
- (3) depreciation and amortization expense of the Company and its consolidated Restricted Subsidiaries (excluding amortization expense attributable to a prepaid operating activity item that was paid in cash in a prior period); and

- (4) all other non-cash charges of the Company and its consolidated Restricted Subsidiaries (excluding any such non-cash charge to the extent that it represents an accrual of or reserve for cash expenditures in any future period);

in each case for such period. Notwithstanding the foregoing, the provision for taxes based on the income or profits of, and the depreciation and amortization and non-cash charges of, a Restricted Subsidiary shall be added to Consolidated Net Income to compute EBITDA only to the extent (and in the same proportion, including by reason of minority interests) that the net income or loss of such Restricted Subsidiary was included in calculating Consolidated Net Income and only if a corresponding amount would be permitted at the date of determination to be dividended to the Company by such Restricted Subsidiary without prior approval (that has not been obtained), pursuant to the terms of its charter and all agreements, instruments, judgments, decrees, orders, statutes, rules and governmental regulations applicable to such Restricted Subsidiary or its stockholders.

“*Equity Offering*” means any sale of Capital Stock (other than Disqualified Stock).

“*Existing Term Loan Agreement*” means the Credit Agreement dated as of November 30, 2006 between the Company and Citibank, N.A., as Administrative Agent and Banco Nacional de Mexico, S.A., Intergrante Del Grupo Financiero Banamex as Peso Agent.

“*Exchange Act*” means the U.S. Securities Exchange Act of 1934, as amended.

“*GAAP*” means Mexican Financial Reporting Standards as in effect on September 22, 2009.

“*Guarantee*” means any obligation, contingent or otherwise, of any Person directly or indirectly guaranteeing any Indebtedness of any Person and any obligation, direct or indirect, contingent or otherwise, of such Person:

- (1) to purchase or pay (or advance or supply funds for the purchase or payment of) such Indebtedness of such Person (whether arising by virtue of partnership arrangements, or by agreements to keep-well, to purchase assets, goods, securities or services, to take-or-pay or to maintain financial statement conditions or otherwise); or
- (2) entered into for the purpose of assuring in any other manner the obligee of such Indebtedness of the payment thereof or to protect such obligee against loss in respect thereof (in whole or in part);

*provided, however*, that the term “Guarantee” shall not include endorsements for collection or deposit in the ordinary course of business. The term “Guarantee” used as a verb has a corresponding meaning.

“*Guaranty Agreement*” means a supplemental indenture, in a form satisfactory to the Trustee, pursuant to which a Subsidiary Guarantor guarantees the Company’s obligations with respect to the Notes on the terms provided for in the Indenture.

“*Hedging Obligations*” of any Person means the obligations of such Person pursuant to any Interest Rate Agreement or Currency Agreement.

“*Holder*” or “*Noteholder*” means the Person in whose name a Note is registered on the Registrar’s books.

“*Incur*” means issue, assume, Guarantee, incur or otherwise become liable for; *provided, however*, that any Indebtedness of a Person existing at the time such Person becomes a Restricted Subsidiary (whether by merger, consolidation, acquisition or otherwise) shall be deemed to be Incurred by such Person at the time it becomes a Restricted Subsidiary. The term “Incurrence” when used as a noun shall have a correlative meaning. Solely for purposes of determining compliance with “—Certain Covenants—Limitation on Indebtedness”:

- (1) amortization of debt discount or the accretion of principal with respect to a non-interest bearing or other discount security;

- (2) the payment of regularly scheduled interest in the form of additional Indebtedness of the same instrument or the payment of regularly scheduled dividends on Capital Stock in the form of additional Capital Stock of the same class and with the same terms; and
- (3) the obligation to pay a premium in respect of Indebtedness arising in connection with the issuance of a notice of redemption or making of a mandatory offer to purchase such Indebtedness will not be deemed to be the Incurrence of Indebtedness.

will not be deemed to be the Incurrence of Indebtedness.

“*Indebtedness*” means, with respect to any Person on any date of determination (without duplication):

- (1) the principal in respect of (A) indebtedness of such Person for money borrowed and (B) indebtedness evidenced by the Notes, debentures, bonds or other similar instruments for the payment of which such Person is responsible or liable, including, in each case, any premium on such indebtedness to the extent such premium has become due and payable;
- (2) all Capital Lease Obligations (other than the Avantel/Telmex IRU and replacements thereof) of such Person and all Attributable Debt in respect of Sale/Leaseback Transactions entered into by such Person;
- (3) all obligations of such Person issued or assumed as the deferred purchase price of property, all conditional sale obligations of such Person and all obligations of such Person under any title retention agreement (but excluding trade accounts payable arising in the ordinary course of business);
- (4) all obligations of such Person for the reimbursement of any obligor on any letter of credit, fianza, bankers’ acceptance or similar credit transaction (other than obligations with respect to letters of credit or fianzas securing obligations (other than obligations described in clauses (1) through (3) above) entered into in the ordinary course of business of such Person to the extent such letters of credit or fianzas are not drawn upon or, if and to the extent drawn upon, such drawing is reimbursed no later than the tenth Business Day following payment on the letter of credit or fianza);
- (5) the amount of all obligations of such Person with respect to the redemption, repayment or other repurchase of any Capital Stock of such Person or any Subsidiary of such Person or that are determined by the value of such Capital Stock, the principal amount of such Capital Stock to be determined in accordance with the Indenture;
- (6) all obligations of the type referred to in clauses (1) through (5) of other Persons and all dividends of other Persons for the payment of which, in either case, such Person is responsible or liable, directly or indirectly, as obligor, guarantor or otherwise, including by means of any Guarantee;
- (7) all obligations of the type referred to in clauses (1) through (6) of other Persons secured by any Lien on any property or asset of such Person (whether or not such obligation is assumed by such Person), the amount of such obligation being deemed to be the lesser of the value of such property or assets and the amount of the obligation so secured; and
- (8) to the extent not otherwise included in this definition, Hedging Obligations of such Person.

Notwithstanding the foregoing, in connection with the purchase by the Company or any Restricted Subsidiary of any business, the term “*Indebtedness*” will exclude post-closing payment adjustments to which the seller may become entitled to the extent such payment is determined by a final closing balance sheet or such payment depends on the performance of such business after the closing;

*provided, however*, that, at the time of closing, the amount of any such payment is not determinable and, to the extent such payment thereafter becomes fixed and determined, the amount is paid within 30 days thereafter.

The amount of Indebtedness of any Person at any date shall be the outstanding balance at such date of all obligations as described above; *provided, however*, that in the case of Indebtedness sold at a discount, the amount of such Indebtedness at any time will be the accreted value thereof at such time.

“*Independent Qualified Party*” means an investment banking firm, accounting firm or appraisal firm of national standing; *provided, however*, that such firm is not an Affiliate of the Company.

“*Interest Rate Agreement*” means any interest rate swap agreement, interest rate cap agreement or other financial agreement or arrangement with respect to exposure to interest rates.

“*Investment*” in any Person means any direct or indirect advance, loan (other than advances to customers in the ordinary course of business that are recorded as accounts receivable on the balance sheet of the lender) or other extensions of credit (including by way of Guarantee or similar arrangement) or capital contribution to (by means of any transfer of cash or other property to others or any payment for property or services for the account or use of others), or any purchase or acquisition of Capital Stock, Indebtedness or other similar instruments issued by such Person. Except as otherwise provided for herein, the amount of an Investment shall be its fair value at the time the Investment is made and without giving effect to subsequent changes in value.

For purposes of the definition of “Unrestricted Subsidiary,” the definition of “Restricted Payment” and the covenant described under “—Certain Covenants—Limitation on Restricted Payments”:

- (1) “Investment” shall include the portion (proportionate to the Company’s equity interest in such Subsidiary) of the fair market value of the net assets of any Subsidiary of the Company at the time that such Subsidiary is designated an Unrestricted Subsidiary; *provided, however*, that upon a redesignation of such Subsidiary as a Restricted Subsidiary, the Company shall be deemed to continue to have a permanent “Investment” in an Unrestricted Subsidiary equal to an amount (if positive) equal to (A) the Company’s “Investment” in such Subsidiary at the time of such redesignation less (B) the portion (proportionate to the Company’s equity interest in such Subsidiary) of the fair market value of the net assets of such Subsidiary at the time of such redesignation; and
- (2) any property transferred to or from an Unrestricted Subsidiary shall be valued at its fair market value at the time of such transfer, in each case as determined in good faith by the Board of Directors.

“*Legal Holiday*” means a Saturday, a Sunday or a day on which banking institutions are not required to be open in the State of New York or the United Mexican States.

“*Lien*” means any mortgage, pledge, security interest, encumbrance, lien or charge of any kind (including any conditional sale or other title retention agreement or lease in the nature thereof).

“*Moody’s*” means Moody’s Investors Service, Inc. and any successor to its rating agency business.

“*Net Available Cash*” from an Asset Disposition means cash payments received therefrom (including any cash payments received by way of deferred payment of principal pursuant to a note or installment receivable or otherwise and proceeds from the sale or other disposition of any securities received as consideration, but only as and when received, but excluding any other consideration received in the form of assumption by the acquiring Person of Indebtedness or other obligations relating to such properties or assets or received in any other non-cash form), in each case net of:

- (1) all legal, title and recording tax expenses, commissions and other fees and expenses incurred, and all Federal, state, provincial, foreign and local taxes required to be accrued as a liability under GAAP, as a consequence of such Asset Disposition;
- (2) all payments made on any Indebtedness which is secured by any assets subject to such Asset Disposition, in accordance with the terms of any Lien upon or other security agreement of any kind with respect to such assets, or which must by its terms, or in order to obtain a necessary consent to such Asset Disposition, or by applicable law, be repaid out of the proceeds from such Asset Disposition;
- (3) all distributions and other payments required to be made to minority interest holders in Restricted Subsidiaries as a result of such Asset Disposition;

- (4) the deduction of appropriate amounts provided by the seller as a reserve, in accordance with GAAP, against any liabilities associated with the property or other assets disposed in such Asset Disposition and retained by the Company or any Restricted Subsidiary after such Asset Disposition; and
- (5) any portion of the purchase price from an Asset Disposition placed in escrow, whether as a reserve for adjustment of the purchase price, for satisfaction of indemnities in respect of such Asset Disposition or otherwise in connection with that Asset Disposition; *provided, however*, that upon the termination of that escrow, Net Available Cash will be increased by any portion of funds in the escrow that are released to the Company or any Restricted Subsidiary.

“*Net Cash Proceeds*,” with respect to any issuance or sale of Capital Stock or Indebtedness, means the cash proceeds of such issuance or sale net of attorneys’ fees, accountants’ fees, underwriters’ or placement agents’ fees, discounts or commissions and brokerage, consultant and other fees actually incurred in connection with such issuance or sale and net of taxes paid or payable as a result thereof.

“*Obligations*” means, with respect to any Indebtedness, all obligations for principal, premium, interest, penalties, fees, indemnifications, reimbursements, and other amounts payable pursuant to the documentation governing such Indebtedness.

“*Officer*” means the Chairman of the Board, the Chief Executive Officer, any Vice President, the Chief Financial Officer, the Treasurer or the Secretary of the Company.

“*Officers’ Certificate*” means a certificate signed by two Officers.

“*Opinion of Counsel*” means a written opinion from legal counsel who is acceptable to the Trustee. The counsel may be an employee of or counsel to the Company or the Trustee.

“*Permitted Asset Swap*” means the disposition by the Company or its Restricted Subsidiaries of Telecommunication Assets to another Person or Persons in exchange for which the Company and the Restricted Subsidiaries receive Telecommunications Assets having, in the reasonable judgment of the disinterested members of the Board of Directors, a fair market value substantially equivalent to or greater than the fair market value of the Telecommunications Assets so disposed; *provided, however*, that if the book value of the Telecommunications Assets to be disposed in a Permitted Asset Swap (or in a series of related Permitted Asset Swaps) exceeds US\$15 million, such disposition shall not constitute a Permitted Asset Swap unless an Independent Qualified Party shall have determined in writing that the fair market value of the Telecommunications Assets to be received by the Company and its Restricted Subsidiaries is substantially equivalent to or greater than the fair market value of the Telecommunications Assets to be disposed.

“*Permitted Holders*” means (a) any Person that is an Affiliate of the Company as of September 22, 2009 (and not established as an Affiliate in order to effect what would otherwise be a Change of Control) and (b) each of the direct shareholders of record of the Company as of September 22, 2009 (as identified in the Indenture), and any Affiliate thereof.

“*Permitted Investment*” means an Investment by the Company or any Restricted Subsidiary in:

- (1) the Company, a Restricted Subsidiary or a Person that will, upon the making of such Investment, become a Restricted Subsidiary; *provided, however*, that the primary business of such Restricted Subsidiary is a Related Business;
- (2) another Person if, as a result of such Investment, such other Person is merged or consolidated with or into, or transfers or conveys all or substantially all its assets to, the Company or a Restricted Subsidiary; *provided, however*, that such Person’s primary business is a Related Business;
- (3) cash and Temporary Cash Investments;



- (4) receivables owing to the Company or any Restricted Subsidiary if created or acquired in the ordinary course of business and payable or dischargeable in accordance with customary trade terms; *provided*, however, that such trade terms may include such concessionary trade terms as the Company or any such Restricted Subsidiary deems reasonable under the circumstances;
- (5) payroll, travel and similar advances to cover matters that are expected at the time of such advances ultimately to be treated as expenses for accounting purposes and that are made in the ordinary course of business;
- (6) loans or advances to employees made in the ordinary course of business consistent with past practices of the Company or such Restricted Subsidiary;
- (7) stock, obligations or securities received in settlement of debts created in the ordinary course of business and owing to the Company or any Restricted Subsidiary or in satisfaction of judgments;
- (8) any Person to the extent such Investment represents the non-cash portion of the consideration received for (A) an Asset Disposition as permitted pursuant to the covenant described under “—Certain Covenants—Limitation on Sales of Assets and Subsidiary Stock” or (B) a disposition of assets not constituting an Asset Disposition;
- (9) any Person where such Investment was acquired by the Company or any of its Restricted Subsidiaries (A) in exchange for any other Investment or accounts receivable held by the Company or any such Restricted Subsidiary in connection with or as a result of a bankruptcy, workout, reorganization or recapitalization of the issuer of such other Investment or accounts receivable or (B) as a result of a foreclosure by the Company or any of its Restricted Subsidiaries with respect to any secured Investment or other transfer of title with respect to any secured Investment in default;
- (10) Persons, to the extent such Investments, when taken together with all other Investments made pursuant to this clause (10) outstanding on the date such Investment is made, do not exceed an amount equal to 20% of Consolidated Net Tangible Assets;
- (11) any Person to the extent such Investments consist of prepaid expenses, negotiable instruments held for collection and lease, utility and workers’ compensation, performance and other similar deposits made in the ordinary course of business by the Company or any Restricted Subsidiary;
- (12) any Person to the extent such Investments consist of Hedging Obligations otherwise permitted under the covenant described under “—Certain Covenants—Limitation on Indebtedness”;
- (13) any Person to the extent such Investment existed on September 22, 2009, and any extension, modification or renewal of any such Investments existing on September 22, 2009, but only to the extent not involving additional advances, contributions or other Investments of cash or other assets or other increases thereof (other than as a result of the accrual or accretion of interest or original issue discount or the issuance of pay-in-kind securities), in each case, pursuant to the terms of such Investment as in effect on September 22, 2009; and
- (14) Persons to the extent such Investments, when taken together with all other Investments made pursuant to this clause (14) outstanding on the date such Investment is made, do not exceed US\$10 million.

“*Permitted Liens*” means, with respect to any Person:

- (1) pledges or deposits by such Person under workers’ compensation laws, unemployment insurance laws or similar legislation, or good faith deposits in connection with bids, tenders, contracts (other than for the payment of Indebtedness) or leases to which such Person is a party, or deposits to secure public or statutory obligations of such Person or deposits of cash or United States government bonds to secure surety or appeal bonds to which such Person is a party, or deposits as security for contested taxes or import duties or for the payment of rent, in each case Incurred in the ordinary course of business;

- (2) Liens imposed by law, such as carriers', warehousemen's and mechanics' Liens, in each case for sums not yet due or being contested in good faith by appropriate proceedings or other Liens arising out of judgments or awards against such Person with respect to which such Person shall then be proceeding with an appeal or other proceedings for review and Liens arising solely by virtue of any statutory or common law provision relating to banker's Liens, rights of set-off or similar rights and remedies as to deposit accounts or other funds maintained with a creditor depository institution; *provided, however*, that (A) such deposit account is not a dedicated cash collateral account and is not subject to restrictions against access by the Company in excess of those set forth by regulations promulgated by the Federal Reserve Board and (B) such deposit account is not intended by the Company or any Restricted Subsidiary to provide collateral to the depository institution;
- (3) Liens for property taxes not yet subject to penalties for non-payment or which are being contested in good faith by appropriate proceedings;
- (4) Liens in favor of issuers of surety bonds or letters of credit issued pursuant to the request of and for the account of such Person in the ordinary course of its business; *provided, however*, that such letters of credit do not constitute Indebtedness;
- (5) minor survey exceptions, minor encumbrances, easements or reservations of, or rights of others for, licenses, rights-of-way, sewers, electric lines, telegraph and telephone lines and other similar purposes, or zoning or other restrictions as to the use of real property or Liens incidental to the conduct of the business of such Person or to the ownership of its properties which were not Incurred in connection with Indebtedness and which do not in the aggregate materially adversely affect the value of said properties or materially impair their use in the operation of the business of such Person;
- (6) Liens securing Indebtedness Incurred to finance the construction, purchase or lease of, or repairs, improvements or additions to, property, plant or equipment of such Person; *provided, however*, that the Lien may not extend to any other property owned by such Person or any of its Restricted Subsidiaries at the time the Lien is Incurred (other than assets and property affixed or appurtenant thereto), and the Indebtedness (other than any interest thereon) secured by the Lien may not be Incurred more than 180 days after the later of the acquisition, completion of construction, repair, improvement, addition or commencement of full operation of the property subject to the Lien;
- (7) Liens existing on September 22, 2009;
- (8) Liens on property or shares of Capital Stock of another Person at the time such other Person becomes a Subsidiary of such Person; *provided, however*, that the Liens may not extend to any other property owned by such Person or any of its Restricted Subsidiaries (other than assets and property affixed or appurtenant thereto);
- (9) Liens on property at the time such Person or any of its Subsidiaries acquires the property, including any acquisition by means of a merger or consolidation with or into such Person or a Subsidiary of such Person; *provided, however*, that the Liens may not extend to any other property owned by such Person or any of its Restricted Subsidiaries (other than assets and property affixed or appurtenant thereto);
- (10) Liens securing Indebtedness or other obligations of a Subsidiary of such Person owing to such Person or a Wholly Owned Subsidiary of such Person;
- (11) Liens securing Hedging Obligations permitted to be Incurred under the Indenture;
- (12) Liens securing directly or indirectly obligations in respect of term loans or revolving loans or other Indebtedness (including principal, premium, interest, penalties, fees, indemnifications, reimbursements and other amounts relating thereto) permitted to be Incurred under the Indenture; *provided, however*, that, at the time of Incurrence of the Indebtedness so secured and after giving effect thereto, the Consolidated Secured Leverage Ratio would be no greater than 2 to 1;

- (13) Liens to secure any Refinancing (or successive Refinancings) as a whole, or in part, of any Indebtedness secured by any Lien referred to in the foregoing clauses (6), (7), (8), (9) and clause (14) below; *provided, however*, that:
- (A) such new Lien shall be limited to all or part of the same property and assets that secured or, under the written agreements pursuant to which the original Lien arose, could secure the original Lien (plus improvements and accessions to, such property or proceeds or distributions thereof); and
  - (B) the Indebtedness secured by such Lien at such time is not increased to any amount greater than the sum of (i) the outstanding principal amount or, if greater, committed amount of the Indebtedness described under clauses (6), (7), (8), (9) or (14) at the time the original Lien became a Permitted Lien and (ii) an amount necessary to pay any fees and expenses, including premiums, related to such refinancing, refunding, extension, renewal or replacement;
- (14) Liens securing Purchase Money Obligations or Capital Lease Obligations Incurred in compliance with the covenant described under “—Certain Covenants—Limitation on Indebtedness”;
- (15) Liens granted by the Company or any Restricted Subsidiary to the Company or any Restricted Subsidiary pursuant to any joint venture agreements;
- (16) Liens in favor of customs and revenues authorities arising as a matter of law to secure customs payments in connection with the importation of goods;
- (17) licenses of patents, trademarks, and other intellectual property rights granted by the Company or any Restricted Subsidiary in the ordinary course of business and not interfering in any material respect with the ordinary conduct of the Company or any Restricted Subsidiary;
- (18) Pledges or deposits of cash and cash equivalents securing deductibles, self-insurance, co-payment, co-insurance, retentions or similar obligations to providers of property, casualty or liability insurance in the ordinary course of business;
- (19) Liens on insurance policies and the proceeds thereof securing the financing of the premiums with respect thereto; and
- (20) licenses, leases, or subleases granted to third Persons or the Company or its Subsidiaries by the Company and/or its Subsidiaries in the ordinary course of business and not interfering in any material respect with the business of the Company and its Restricted Subsidiaries.

Notwithstanding the foregoing, “Permitted Liens” will not include any Lien described in clauses (6), (8), (9) or (14) above to the extent such Lien applies to any Additional Assets acquired directly or indirectly from Net Available Cash pursuant to the covenant described under “—Certain Covenants—Limitation on Sale of Assets and Subsidiary Stock.” For purposes of this definition, the term “Indebtedness” shall be deemed to include interest on such Indebtedness.

“*Person*” means any individual, corporation, partnership, limited liability company, joint venture, association, joint-stock company, trust, unincorporated organization, government or any agency or political subdivision thereof or any other entity.

“*Pesos*” means the legal currency of the United Mexican States.

“*Preferred Stock*,” as applied to the Capital Stock of any Person, means Capital Stock of any class or classes (however designated) which is preferred as to the payment of dividends or distributions, or as to the distribution of assets upon any voluntary or involuntary liquidation or dissolution of such Person, over shares of Capital Stock of any other class of such Person.

“*principal*” of a Note means the principal of the Note plus the premium, if any, payable on the Note which is due or overdue or is to become due at the relevant time.

“*Purchase Money Obligations*” means any Indebtedness Incurred to finance or refinance the acquisition, leasing, construction or improvement of property (real or personal) or assets, and whether acquired through the direct acquisition of such property or assets or the Capital Stock of any Person owning such property or assets, or otherwise.

“*Refinance*” means, in respect of any Indebtedness, to refinance, extend, renew, refund, repay, prepay, purchase, redeem, defease or retire, or to issue other Indebtedness in exchange or replacement for, such Indebtedness.

“*Refinanced*” and “*Refinancing*” shall have correlative meanings.

“*Refinancing Indebtedness*” means Indebtedness that Refinances any Indebtedness of the Company or any Restricted Subsidiary existing on September 22, 2009 or Incurred in compliance with the Indenture, including Indebtedness that Refinances Refinancing Indebtedness; *provided, however*, that:

- (1) such Refinancing Indebtedness has a Stated Maturity no earlier than the Stated Maturity of the Indebtedness being Refinanced;
- (2) such Refinancing Indebtedness has an Average Life at the time such Refinancing Indebtedness is Incurred that is equal to or greater than the Average Life of the Indebtedness being Refinanced;
- (3) such Refinancing Indebtedness has an aggregate principal amount (or if Incurred with original issue discount, an aggregate issue price) that is equal to or less than the aggregate principal amount (or if Incurred with original issue discount, the aggregate accreted value) then outstanding or committed (plus fees and expenses, including any premium and defeasance costs) under the Indebtedness being Refinanced; and
- (4) if the Indebtedness being Refinanced is subordinated in right of payment to the Notes, such Refinancing Indebtedness is subordinated in right of payment to the Notes at least to the same extent as the Indebtedness being Refinanced;

*provided further, however*, that Refinancing Indebtedness shall not include (A) Indebtedness of a Subsidiary that Refinances Indebtedness of the Company or (B) Indebtedness of the Company or a Restricted Subsidiary that Refinances Indebtedness of an Unrestricted Subsidiary.

“*Related Business*” means any business in which the Company or any of the Restricted Subsidiaries was engaged on September 22, 2009 and any business related, ancillary or complementary to such business.

“*Restricted Payment*” with respect to any Person means:

- (1) the declaration or payment of any dividends or any other distributions of any sort in respect of its Capital Stock (including any payment in connection with any merger or consolidation involving such Person) or similar payment to the direct or indirect holders of its Capital Stock (other than (A) dividends or distributions payable solely in its Capital Stock (other than Disqualified Stock), (B) dividends or distributions payable solely to the Company or a Restricted Subsidiary and (C) pro rata dividends or other distributions made by a Subsidiary that is not a Wholly Owned Subsidiary to minority stockholders (or owners of an equivalent interest in the case of a Subsidiary that is an entity other than a corporation));
- (2) the purchase, redemption or other acquisition or retirement for value of any Capital Stock of the Company held by any Person (other than by a Restricted Subsidiary) or of any Capital Stock of a Restricted Subsidiary held by any Affiliate of the Company (other than by a Restricted Subsidiary), including in connection with any merger or consolidation and including the exercise of any option to exchange any Capital Stock (other than into Capital Stock of the Company that is not Disqualified Stock);

- (3) the purchase, repurchase, redemption, defeasance or other acquisition or retirement for value, prior to scheduled maturity, scheduled repayment or scheduled sinking fund payment of any Subordinated Obligations of the Company or any Subsidiary Guarantor (other than (A) from the Company or a Restricted Subsidiary or (B) the purchase, repurchase, redemption, defeasance or other acquisition of Subordinated Obligations purchased in anticipation of satisfying a sinking fund obligation, principal installment or final maturity, in each case due within one year of the date of such purchase, repurchase, redemption, defeasance or other acquisition); or
- (4) the making of any Investment (other than a Permitted Investment) in any Person.

“*Restricted Subsidiary*” means any Subsidiary of the Company that is not an Unrestricted Subsidiary.

“*Sale/Leaseback Transaction*” means an arrangement relating to property owned by the Company or a Restricted Subsidiary on September 22, 2009 or thereafter acquired by the Company or a Restricted Subsidiary whereby the Company or a Restricted Subsidiary transfers such property to a Person and the Company or a Restricted Subsidiary leases it from such Person.

“*SEC*” means the U.S. Securities and Exchange Commission.

“*Securities Act*” means the U.S. Securities Act of 1933, as amended.

“*Senior Indebtedness*” means with respect to any Person:

- (1) Indebtedness of such Person, whether outstanding on September 22, 2009 or thereafter Incurred; and
- (2) all other Obligations of such Person (including interest accruing on or after the filing of any petition in bankruptcy or for reorganization relating to such Person whether or not post-filing interest is allowed in such proceeding) in respect of Indebtedness described in clause (1) above unless, in the case of clauses (1) and (2), in the instrument creating or evidencing the same or pursuant to which the same is outstanding, it is *provided* that such Indebtedness or other obligations are subordinate in right of payment to the Notes or the Subsidiary Guaranty of such Person, as the case may be; *provided, however*, that Senior Indebtedness shall not include:
  - (a) any obligation of such Person to the Company or any Subsidiary;
  - (b) any liability for any national, state, local or other taxes owed or owing by such Person;
  - (c) any accounts payable or other liability to trade creditors arising in the ordinary course of business (including guarantees thereof or instruments evidencing such liabilities);
  - (d) any Indebtedness or other Obligation (and any accrued or unpaid interest in respect thereof) of such Person which is subordinate or junior in any respect to any other Indebtedness or other Obligation of such Person; or
  - (e) that portion of any Indebtedness which at the time of Incurrence is Incurred in violation of the Indenture.

“*Significant Subsidiary*” means any Restricted Subsidiary that would be a “Significant Subsidiary” of the Company within the meaning of Rule 1-02 under Regulation S-X promulgated by the SEC.

“*Standard & Poor’s*” means Standard & Poor’s, a division of The McGraw-Hill Companies, Inc., and any successor to its rating agency business.

“*Stated Maturity*” means, with respect to any security, the date specified in such security as the fixed date on which the final payment of principal of such security is due and payable, including pursuant to any mandatory redemption provision (but excluding any provision providing for the repurchase of such security at the option of the holder thereof upon the happening of any contingency unless such contingency has occurred).

“*Subordinated Obligation*” means, with respect to a Person, any Indebtedness of such Person (whether outstanding on September 22, 2009 or thereafter Incurred) which is subordinate or junior in right of payment to the Notes or a Subsidiary Guaranty of such Person, as the case may be, pursuant to a written agreement to that effect.

“*Subsidiary*” means, with respect to any Person, any corporation, association, partnership or other business entity of which more than 50% of the total voting power of shares of Voting Stock is at the time owned or controlled, directly or indirectly, by:

- (1) such Person;
- (2) such Person and one or more Subsidiaries of such Person; or
- (3) one or more Subsidiaries of such Person.

“*Subsidiary Guaranty*” means a Guarantee by a Subsidiary Guarantor of the Company’s obligations with respect to the Securities.

“*Subsidiary Guarantor*” means Instalaciones y Contrataciones, S.A. de C.V., Servicios Axtel, S.A. de C.V., Avantel Infraestructura, S. de R.L. de C.V. and Avantel, S. de R.L. de C.V. and each other Restricted Subsidiary of the Company that executes the Indenture as a guarantor on September 22, 2009 and each Restricted Subsidiary of the Company that thereafter guarantees the Notes pursuant to the terms of the Indenture, in each case unless and until such Restricted Subsidiary is released from its obligation under its Subsidiary Guaranty pursuant to the terms of the Indenture.

“*Telecommunications Assets*” means any property, including licenses and applications, bids and agreements to acquire licenses, or other authority to provide telecommunications services, used or intended for use primarily in connection with a Related Business.

“*Temporary Cash Investments*” means any of the following:

- (1) securities issued or directly and fully guaranteed by the United States government or any agency or instrumentality thereof with a maturity of less than one year;
- (2) certificates of deposit and Eurodollar time deposits with a maturity of not later than six months, bankers’ acceptances with a maturity of not later than six months and overnight bank deposits, in each case with any U.S. commercial bank of recognized stature having capital and surplus in excess of US\$500,000,000 and having a commercial paper rating (or the holding company thereof having a commercial paper rating) of “A-1” or better by Standard & Poor’s or “P-1” or better by Moody’s, and that is a member of the Federal Reserve System;
- (3) commercial paper rated “A-1” or better by Standard & Poor’s or “P-1” or better by Moody’s with maturity of less than one year;
- (4) guaranteed investment contracts with a maturity of less than one year and entered into with (or fully guaranteed by) financial institutions whose long-term unsecured non-credit enhanced indebtedness is rated “A-” or better by Standard & Poor’s or “A2” or better by Moody’s;
- (5) Investments in money market funds having a rating from each of Standard & Poor’s and Moody’s in the highest investment category granted thereby;
- (6) obligations with a maturity of less than one year that are direct obligations of the Mexican government or of entities having the statutory guarantee of the Mexican government, or obligations that are expressly and unconditionally guaranteed by the Mexican government;
- (7) obligations with a maturity of less than one year of Mexican commercial banks of recognized stature, supervised by the Mexican National Banking and Securities Commission, with a capital and surplus of



at least US\$250,000,000 (or its equivalent in other currencies); *provided* that the aggregate Investments of the Credit Parties in Mexican commercial banks not having Mexican domestic ratings of AA+(mex) or above from Fitch and mxA+ or above from Standard & Poor's shall not exceed US\$25,000,000 (or its equivalent in Pesos) at any time;

- (8) commercial paper of Mexican corporations with a maturity of less than one year and rated at least "A3" by Standard & Poor's;
- (9) repurchase agreements with a maturity of less than one year, in each case related to any of the Investments described in (6) through (8), and that are fully collateralized by such Investments, with any Mexican commercial bank that meets the criteria outlined in clause (7); *provided* that the aggregate amount invested in such repurchase agreements shall not exceed US\$25,000,000 (or its equivalent in Pesos) at any time.

"*Trustee*" means The Bank of New York Mellon until a successor replaces it and, thereafter, means the successor.

"*Trust Indenture Act*" means the Trust Indenture Act of 1939 (15 U.S.C. §§ 77aaa-77bbb) as in effect on September 22, 2009.

"*Trust Officer*" means any officer of the Trustee with direct responsibility for the administration of the Indenture and also, with respect to a particular matter, any other officer of the Trustee to whom such matter is referred because of such officer's knowledge and familiarity with the particular subject.

"*Unrestricted Subsidiary*" means:

- (1) Telecom Networks, Inc.;
- (2) any Subsidiary of the Company that at the time of determination shall be designated an Unrestricted Subsidiary by the Board of Directors in the manner provided below; and
- (3) any Subsidiary of an Unrestricted Subsidiary.

The Board of Directors may designate any Subsidiary of the Company (including any newly acquired or newly formed Subsidiary of the Company) to be an Unrestricted Subsidiary unless such Subsidiary or any of its Subsidiaries owns any Capital Stock or Indebtedness of, or holds any Lien on any property of, the Company or any other Subsidiary of the Company that is not a Subsidiary of the Subsidiary to be so designated; *provided, however,* that either (A) the Subsidiary to be so designated has total assets of US\$1,000 or less or (B) if such Subsidiary has assets greater than US\$1,000, such designation would be permitted under the covenant described under "—Certain Covenants—Limitation on Restricted Payments."

The Board of Directors may designate any Unrestricted Subsidiary to be a Restricted Subsidiary; *provided, however,* that immediately after giving effect to such designation (A) the Company could Incur US\$1.00 of additional Indebtedness under paragraph (a) of the covenant described under "—Certain Covenants—Limitation on Indebtedness" and (B) no Default shall have occurred and be continuing. Any such designation by the Board of Directors shall be evidenced to the Trustee by promptly filing with the Trustee a copy of the resolution of the Board of Directors giving effect to such designation and an Officers' Certificate certifying that such designation complied with the foregoing provisions.

"*US Dollar Equivalent*" means with respect to any monetary amount in a currency other than US dollars, at any time for determination thereof, the amount of US dollars obtained by converting such foreign currency involved in such computation into US dollars at the spot rate for the purchase of US dollars with the applicable foreign currency as published in The Wall Street Journal in the "Exchange Rates" column under the heading "Currency Trading" on the date two Business Days prior to such determination.

Except as described under “—Certain Covenants—Limitation on Indebtedness,” whenever it is necessary to determine whether the Company has complied with any covenant in the Indenture or a Default has occurred and an amount is expressed in a currency other than US dollars, such amount will be treated as the US Dollar Equivalent determined as of the date such amount is initially determined in such currency.

“*US Government Obligations*” means direct obligations (or certificates representing an ownership interest in such obligations) of the United States of America (including any agency or instrumentality thereof) for the payment of which the full faith and credit of the United States of America is pledged and which are not callable at the issuer’s option.

“*Voting Stock*” of a Person means all classes of Capital Stock of such Person then outstanding and normally entitled (without regard to the occurrence of any contingency) to vote in the election of directors, managers or trustees thereof.

“*Wholly Owned Subsidiary*” means a Restricted Subsidiary all the Capital Stock of which (other than directors’ qualifying shares or an immaterial amount of shares required to be owned by other Persons pursuant to Mexican law) is owned, directly or indirectly, by the Company or one or more other Wholly Owned Subsidiaries.

## CERTAIN UNITED STATES FEDERAL INCOME TAX CONSEQUENCES

The following is a general summary of certain U.S. federal income tax consequences associated with the purchase, beneficial ownership and disposition of the new notes by U.S. holders (as defined below). This summary is based on the U.S. Internal Revenue Code of 1986, as amended (the “Code”), Treasury regulations promulgated thereunder, rulings, official pronouncements and judicial decisions, all as in effect on the date of this offering circular and all of which are subject to change, possibly with retroactive effect, or different interpretations. This summary only addresses tax considerations for holders that purchase the new notes pursuant to this offering at the original issue price and that hold the new notes as “capital assets” (generally, property held for investment). Moreover, this summary is for general information only and does not address all of the tax consequences that may be relevant to specific investors in light of their particular circumstances or to investors subject to special treatment under U.S. federal income tax laws (such as Holders other than U.S. holders, banks, insurance companies, tax-exempt entities, retirement plans, dealers in securities, brokers, expatriates, entities treated as partnerships for U.S. federal income tax purposes and investors therein, persons who hold their new notes as part of a straddle, hedge, conversion transaction or other integrated investment, U.S. holders whose functional currency is not the U.S. dollar, persons subject to the alternative minimum tax or persons deemed to sell the new notes under the constructive sale provisions of the Code), all of whom may be subject to tax rules that differ significantly from those summarized below. The discussion below does not address U.S. federal estate and gift tax considerations or the effect of any U.S. state, local or non-U.S. tax law. The Company has not sought any ruling from the Internal Revenue Service (the “IRS”) or an opinion of counsel with respect to the statements made and the conclusions reached in this discussion, and there can be no assurance that the IRS will agree with such statements and conclusions.

HOLDERS OF THE NEW NOTES ARE URGED TO CONSULT THEIR OWN TAX ADVISORS AS TO THE PARTICULAR TAX CONSIDERATIONS FOR THEM RELATING TO THE PURCHASE, OWNERSHIP AND DISPOSITION OF THE NEW NOTES, INCLUDING THE APPLICABILITY OF U.S. FEDERAL, STATE OR LOCAL TAX LAWS OR NON-U.S. TAX LAWS, ANY CHANGES IN APPLICABLE TAX LAWS AND ANY PENDING OR PROPOSED LEGISLATION OR REGULATIONS.

**TO ENSURE COMPLIANCE WITH TREASURY DEPARTMENT CIRCULAR 230, YOU ARE HEREBY NOTIFIED THAT: (A) ANY DISCUSSION OF U.S. FEDERAL TAX ISSUES IN THIS OFFERING CIRCULAR IS NOT INTENDED OR WRITTEN BY US TO BE RELIED UPON, AND CANNOT BE RELIED UPON, BY HOLDERS FOR THE PURPOSE OF AVOIDING PENALTIES UNDER THE CODE; (B) SUCH DISCUSSION IS WRITTEN IN CONNECTION WITH THE ISSUER’S PROMOTION OR MARKETING OF THE NEW NOTES; AND (C) HOLDERS SHOULD SEEK ADVICE BASED ON THEIR PARTICULAR CIRCUMSTANCES FROM AN INDEPENDENT TAX ADVISOR.**

For purposes of this summary, a “U.S. holder” is a beneficial holder of a note that is, for U.S. federal income tax purposes:

- an individual who is a citizen or resident of the United States;
- a corporation created or organized in or under the laws of the United States, any state thereof or the District of Columbia;
- an estate the income of which is subject to U.S. federal income tax regardless of the source thereof; or
- a trust (1) if a court within the United States is able to exercise primary supervision over its administration and one or more U.S. persons have the authority to control all of its substantial decisions, or (2) if it validly elects to be treated as a United States person for U.S. federal income tax purposes.

If an entity treated as a partnership for U.S. federal income tax purposes is a beneficial owner of a note, the treatment of a partner in the partnership generally will depend upon the status of the partner and the activities of the partnership.

## **Payment of Interest**

A U.S. holder must include in the U.S. holder's gross income all payments of interest in respect of the new notes, and additional amounts, if any, on account of non-U.S. withholding taxes (in each case, without reduction for any such taxes withheld), at the time accrued or paid, in accordance with the U.S. holder's usual method of tax accounting for U.S. federal income tax purposes.

Because a U.S. holder's interest income will not be reduced by the non-U.S. taxes withheld, a U.S. holder generally will be required to include more interest in the U.S. holder's gross income than the U.S. holder actually receives in cash interest. For U.S. federal income tax purposes, interest on the new notes (including any Additional Amounts) generally will (i) be treated as foreign source income and (ii) constitute passive income, or in the case of certain U.S. holders, general category income. A U.S. holder may be eligible to claim either a U.S. federal income tax deduction or a credit for Mexican taxes withheld from interest paid on the new notes, subject to some limitations (including that the election to deduct or credit foreign taxes applies to all of your foreign taxes for a particular tax year). The rules relating to foreign tax credits are extremely complex and U.S. holders should consult with their own tax advisors regarding the availability of a foreign tax credit and the application of the foreign tax credit limitations to their particular situations.

## **Sale, Exchange, Redemption, Retirement or Other Dispositions**

A U.S. holder generally will recognize gain or loss for U.S. federal income tax purposes upon the sale, exchange, redemption, retirement or other taxable disposition of the new notes in an amount equal to the difference between the amount realized and the U.S. holder's adjusted tax basis in the new notes. For this purpose, the amount realized does not include any amount attributable to accrued interest on the new notes (including any Additional Amounts in respect thereof, which will be taxable as ordinary income as described above, to the extent not previously so taxed), but would include any redemption premium and any Additional Amounts attributable thereto. A U.S. holder's tax basis in the new notes generally will equal the cost of such new notes to such holder.

The gain or loss upon the sale, exchange, redemption, retirement or other disposition of the new notes generally will be capital gain or loss. If, at the time of such disposition, the new notes have been held for more than one year, the gain or loss will be a long-term capital gain or loss. Under current law, long-term capital gains recognized by individuals or other non-corporate U.S. holders are generally subject to a reduced U.S. federal income tax rate. Capital losses are subject to limits on deductibility. Any gain or loss recognized by a U.S. holder generally will be treated as from sources within the United States for U.S. federal income tax purposes, unless the applicable provisions of the U.S.-Mexican income tax treaty provides otherwise. You should consult your own tax advisor regarding the possibility of claiming foreign tax credits for Mexican withholding taxes imposed with respect to any redemption premium.

## **Backup Withholding and Information Reporting**

U.S. backup withholding (at a current rate of 28%) may apply to payments to a U.S. holder of interest on the new notes and/or proceeds from the sale, redemption or retirement of the new notes if the U.S. holder fails to furnish to the paying agent the U.S. holder's taxpayer identification number, that is, the U.S. holder's social security number or employer identification number, or fails to otherwise comply with the applicable requirements of the backup withholding rules. Some U.S. holders, including corporations, are not subject to backup withholding. In addition, payments of interest on the new notes and/or proceeds from the sale, redemption or retirement of the new notes will generally be subject to information reporting requirements.

Any amounts withheld under the backup withholding rules from a payment to a U.S. holder with respect to the new notes will be allowed as a refund or credit against such U.S. holder's U.S. federal income tax liability; *provided* that the U.S. holder timely furnishes the required information to the IRS.

## MATERIAL MEXICAN TAX CONSEQUENCES

The following is a general summary of the principal Mexican federal income tax consequences of the acquisition, ownership and disposition of the new notes by holders that are not residents of Mexico for Mexican federal tax purposes and that do not have a permanent establishment in Mexico (a “foreign holder”). This summary is based on the Mexican federal income tax law (*Ley del Impuesto sobre la Renta*) and regulations thereunder as in effect on the date of this offering circular, all of which are subject to change, possibly with retroactive effect, or different interpretations. This summary does not address all of the tax consequences that may be applicable to specific holders of the new notes and does not purport to be a comprehensive description of all the tax considerations that may be relevant to a decision to purchase, own or dispose of the new notes.

Potential investors are urged to consult with their own tax advisor regarding the particular consequences to them of an investment (including the purchase, ownership or disposition) in the new notes under the laws of Mexico or any other jurisdiction in which they may be subject to tax.

For purposes of Mexican taxation, an individual or corporation that does not satisfy the requirements to be considered a resident of Mexico for tax purposes, specified below, is deemed a non-resident of Mexico for tax purposes. An individual is a resident of Mexico if the individual establishes his/her home in Mexico. When such individual also has a home in another country, he shall be deemed to be a resident of Mexico if his/her “center of vital interest” is in Mexico. In accordance with Mexican Tax Laws, it shall be considered that the individual has his/her center of vital interest in Mexico, when (a) more than the 50% of the total income obtained by such individual in the respective calendar year comes from Mexican sources; or (b) Mexico is the principal center of his professional activities. Mexican citizens who filed a change of tax residence to a country or jurisdiction in which his/her income is subject to a preferential tax regime pursuant to the provisions of the Mexican Income Tax Law will be considered a resident of Mexico for tax purposes during the year of filing the applicable notice of tax residence status with the Mexican tax authorities, and the three immediate following years. Mexican citizens acting as government officials and employees are also residents of Mexico for tax purposes even if their center of vital interest is located outside Mexico. A legal entity is a resident of Mexico if it maintains the principal administration of its business or the effective location of its management in Mexico. A Mexican citizen is presumed to be resident of Mexico unless such person can demonstrate otherwise. If a legal entity or an individual is deemed to have a permanent establishment in Mexico for Mexican tax purposes, all income attributable to that permanent establishment will be subject to Mexican taxes, in accordance with applicable tax laws.

The summary description of the Mexican federal income tax laws set forth below is based on the laws in force as of the date of this offering circular and is subject to any changes in applicable Mexican tax laws. The governments of the United States and Mexico ratified an income tax treaty and protocol which came into effect on January 1, 1994 (the U.S.-Mexico Tax Treaty). The United States and Mexico have also entered into an agreement that covers the exchange of information with respect to tax matters.

Mexico has also entered into and is negotiating tax treaties for the avoidance of double taxation with several other countries.

Each prospective holder of a new note should consult such holder’s tax advisors with respect to the tax treatment applicable to that holder.

This summary of some Mexican income tax considerations deals only with holders of the new notes that are foreign holders.

## Payment of Interest

Pursuant to Article 195, Section II, paragraph (a) of the Mexican Income Tax Law, payments of interest to foreign holders will be subject to Mexican withholding tax at a rate of 4.9%, if, as expected, the following requirements are met:

- we duly and timely file the applicable notice regarding this financing transaction and the issuance of the new notes with the National Banking and Securities Commission (*Comisión Nacional Bancaria y de Valores*), in the terms provided by the Mexican Stock Exchange Law (*Ley del Mercado de Valores*);
- the new notes are placed outside of Mexico through banks or brokerage houses in a country with which Mexico has in force a treaty for avoidance of double taxation (which currently includes the United States of America); and
- we timely file with the Tax Administration Service (*Servicio de Administración Tributaria of the Mexican Secretaría de Hacienda y Crédito Público*), fifteen days after the placement of the new notes, information regarding such placement, and on a quarterly basis, information, among other things, setting forth that no party related to us, jointly or individually, directly or indirectly, is the effective beneficiary of more than 5.0% of the aggregate amount of each interest payment, and we maintain records that evidence compliance with this requirement.

If any of the above-mentioned requirements is not met, the Mexican withholding tax will be 10.0% or higher.

Neither the 4.9% rate nor the 10.0% rate will apply and, therefore, higher withholding tax rates will apply if the effective beneficiaries, directly or indirectly, individually or jointly with related parties, receive more than 5.0% of the interest paid on the new notes and (1) own directly or indirectly, individually or jointly with related parties, more than 10.0% of our voting stock or (2) are entities 20.0% or more of whose stock is owned directly or indirectly, individually or jointly, by parties related to us.

As of the date of this offering circular, the U.S.-Mexico Tax Treaty is not expected to have any material effect on the Mexican tax consequences described herein, because, as described above, under Mexico's income tax law, we will be entitled to withhold taxes in connection with interest payments under the new notes at a 4.9% rate.

Payments of interest on the new notes to non-Mexican pension and retirement funds will be exempt from Mexican withholding tax *provided* that:

- such fund is duly incorporated pursuant to the laws of its country of residence and is the effective beneficiary of the interest payment;
- such income is exempt from taxes in its country of residence;
- such fund is registered with the Ministry of Finance and Public Credit for these purposes; and
- holders or beneficial owners of the new notes, subject to specified exceptions and limitations, may be requested to provide certain information or documentation necessary to enable us and the guarantors to apply the appropriate Mexican withholding tax rate on interest payments made by us or the guarantors to such holders or beneficial owners under the new notes. In the event that the specified information or documentation concerning the holder or beneficial owner, if requested, is not timely provided, we or the guarantors may withhold Mexican tax from interest payments on the new notes to that holder or beneficial owner at the maximum applicable rate, but our obligation to pay Additional Amounts relating to those withholding taxes will be limited as described under "Description of the Notes—Additional Amounts."



**Payment of Principal**

Under Mexican Income Tax Law, principal paid to a foreign holder of the new notes by us is not subject to Mexican withholding tax or similar taxes.

**Acquisition and Disposition of the New Notes**

Gains resulting from the sale or other disposition of our new notes by a foreign holder when the purchaser is a resident of Mexico or a non-resident with a permanent establishment in Mexico will be considered as interest for Mexican tax purposes and, therefore, subject to income tax in Mexico by applying the corresponding withholding tax rates mentioned above. In such case, the difference between the sales price over the sum of the face value will be considered as interest.

Likewise, the Mexican Income Tax Law will impose a withholding tax upon the acquisition at discount of a note by a purchaser that is a non-resident of Mexico for tax purposes, to the extent that the seller is a resident of Mexico or a non-resident with a permanent establishment in Mexico. In such case, the difference between the sales price over the sum of the face value and the accrued interest pending payment will be considered as interest for Mexican tax purposes.

**Taxation of Make-Whole Premium**

Under the Mexican Income Tax Law and regulations thereunder, the payment of the “make-whole” premium as a result of the optional redemption of the new notes, as provided for in the Section “Description of the Notes—Optional Redemption,” will have the same tax treatment as interest payments as provided for in “Payments of Interest” above.

**Other Mexican Taxes**

There are no Mexican estate, inheritance, succession or gift taxes generally applicable to the acquisition, ownership or disposition of the new notes by foreign holders. There are no Mexican stamp, issuer registration or similar taxes or duties payable by foreign holders of the new notes.

## PLAN OF DISTRIBUTION

Under the terms and subject to the conditions contained in a purchase agreement dated March 11, 2010, we have agreed to sell to the initial purchasers, and such initial purchasers have agreed to purchase from us, the principal amount of the new notes set forth opposite their names in the table below.

<b>Initial Purchasers</b>	<b>Principal Amount of New Notes</b>
Credit Suisse Securities (USA) LLC.....	US\$114,000,000
Banc of America Securities LLC .....	US\$ 76,000,000
Total .....	US\$190,000,000

The purchase agreement provides that the initial purchasers are obligated to purchase all of the new notes if any are purchased. The purchase agreement also provides that if any of the initial purchasers defaults, the purchase commitments of non-defaulting initial purchasers may be increased or the offering may be terminated.

The initial purchasers propose to offer the new notes initially at the offering price on the cover page of this offering circular and may also offer the new notes to selling group members at the offering price less a concession. After the initial offering, the offering price may be changed.

The new notes have not been registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except to qualified institutional buyers in reliance on Rule 144A under the Securities Act. The initial purchasers have agreed that, except as permitted by the purchase agreement, they will not offer, sell or deliver the new notes (i) as part of its distribution at any time or (ii) otherwise until 40 days after the later of the commencement of this offering and the closing date, within the United States or to, or for the account or benefit of, U.S. persons, and they will have sent to each broker/dealer to which they sell the new notes in reliance on Regulation S during such 40-day period, a confirmation or other notice detailing the restrictions on offers and sales of the new notes within the United States, or to, or for the account or benefit of, U.S. persons. Terms used in this paragraph have the meanings given to them by Regulation S under the Securities Act. Resales of the new notes are restricted as described under “Transfer Restrictions.”

In addition, until 40 days after the commencement of this offering, an offer or sale of the new notes within the United States by a broker/dealer (whether or not it is participating in the offering), may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than pursuant to Rule 144A.

### **European Economic Area**

Each of the initial purchasers severally represents and agrees that, in relation to each member state of the EEA which has implemented the Prospectus Directive (each, a “Relevant Member State”), each initial purchaser has represented and agreed that with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the “Relevant Implementation Date”) it has not made and will not make an offer of the new notes to the public in that Relevant Member State prior to the publication of a prospectus in relation to the new notes which has been approved by the competent authority in that Relevant Member State or, where appropriate, approved in another Relevant Member State and notified to the competent authority in that Relevant Member State, all in accordance with the Prospectus Directive, except that it may, with effect from and including the Relevant Implementation Date, make an offer of new notes to the public in that Relevant Member State at any time:

- to legal entities which are authorized or regulated to operate in the financial markets or, if not so authorized or regulated, whose corporate purpose is solely to invest in securities;

- to any legal entity which has two or more of (1) an average of at least 250 employees during the last financial year; (2) a total balance sheet of more than €43,000,000 and (3) an annual net turnover of more than €50,000,000, as shown in its last annual or consolidated accounts; or
- in any other circumstances which do not require the publication by us of a prospectus pursuant to Article 3 of the Prospectus Directive.

For the purposes of this provision, the expression an “offer of new notes to the public” in relation to any new notes in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the new notes to be offered so as to enable an investor to decide to purchase or subscribe the new notes, as the same may be varied in that member state by any measure implementing the Prospectus Directive in that member state. The EEA selling restriction is in addition to any other selling restrictions set out below.

### **United Kingdom**

Each of the initial purchasers severally represents and agrees that:

- it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000, or FSMA), received by it in connection with the issue or sale of any new notes in circumstances in which section 21(1) of the FSMA does not apply to us; and
- it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the new notes in, from or otherwise involving the United Kingdom.

### **General**

Each of the initial purchasers has represented and agreed that it has not offered, sold or delivered and will not offer, sell or deliver any new notes directly or indirectly, or distribute this offering circular or any other offering material relating to the new notes in or from any jurisdiction, except under circumstances that will result in compliance with the applicable laws and regulations thereof and that will not impose any obligations on us except as set forth in the purchase agreement.

Purchasers of new notes sold outside the United States may be required to pay stamp taxes and other charges in compliance with the laws and practices of the country of purchase in addition to the price to investors on the cover page of this offering circular.

The initial purchasers and their respective affiliates have provided, and may provide in the future, investment banking, commercial banking, financial advisory and lending services for us and our affiliates from time to time, for which they have received, or will receive, customary compensation. Credit Suisse Securities (USA) LLC served as lead bookrunner and initial purchaser in connection with our offerings of our 13% senior notes due 2013 in December 2003 and January 2005, our 7 5/8% senior unsecured notes due 2017 in January 2007, our 9.0% senior unsecured notes due 2019 in September 2009 and our Series B shares in December 2005, and acted as dealer manager in connection with the tender for our 11.0% senior notes due 2013 in September 2009. In addition, affiliates of Credit Suisse Securities (USA) LLC own 59,500,000 certificados de participación ordinarios (CPO's) (equal to 417,900,000 ordinary shares), which represent 4.75% of our entire capital stock. See “Principal Shareholders.” Bank of America Mexico, S.A Institucion de Banca Multiple, Grupo Financiero Bank of America, affiliates of Banc of America Securities LLC, are lenders under our 2012 Term Loan, and as such are entitled to be repaid with the proceeds of the new notes that will be used to prepay our 2012 Term Loan Facility. Bank of America, N.A., an affiliate of Banc of America Securities LLC, may serve as administrative agent and lender under the New Revolving Credit Facility if and when it is consummated. See “Summary—Recent Developments.” Banc of America Securities LLC was a bookrunner and initial purchaser in connection

with the offering of our 9% senior unsecured notes due 2019 in September 2009. We expect to use a portion of the net proceeds from this offering to (i) to prepay US\$105 million of the aggregate principal amount of indebtedness outstanding under our 2012 Term Loan Facility, (ii) to repay approximately US\$32 million of our short-term indebtedness under the Banamex Promissory Note, (iii) to fund approximately US\$30 million of principal installments on our indebtedness that will become due during 2010, and (iv) for general corporate purposes, capital investments and working capital requirements.

We have agreed to indemnify the initial purchasers against certain liabilities or to contribute to payments which it may be required to make in that respect.

The new notes are a new issue of securities for which there currently is no market. The initial purchasers have advised us that they intend to make a market in the new notes as permitted by applicable law. They are not obligated, however, to make a market in the new notes and any market-making may be discontinued at any time at their sole discretion. Accordingly, no assurance can be given as to the development or liquidity of any market for the new notes.

We expect that delivery of the new notes will be made against payment therefor on or about the closing date specified on the cover page of this offering circular, which will be the seventh business day following the trade date (such settlement being referred to as "T+7").

The initial purchasers may engage in over-allotment, stabilizing transactions, covering transactions and penalty bids in accordance with Regulation M under the Exchange Act.

- Over-allotment involves sales in excess of the offering size, which creates a short position for the initial purchasers.
- Stabilizing transactions permit bids to purchase the underlying security so long as the stabilizing bids do not exceed a specified maximum.
- Covering transactions involve purchases of the new notes in the open market after the distribution has been completed in order to cover short positions.
- Penalty bids permit the initial purchasers to reclaim a selling concession from a broker/dealer when the new notes originally sold by such broker/dealer are purchased in a stabilizing or covering transaction to cover short positions.

These stabilizing transactions, covering transactions and penalty bids may cause the price of the new notes to be higher than they would otherwise be in the absence of these transactions. These transactions, if commenced, may be discontinued at any time.

## TRANSFER RESTRICTIONS

The new notes have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. Accordingly, the new notes are being offered hereby only (a) to “qualified institutional buyers” (as defined in Rule 144A under the Securities Act), or QIBs, in compliance with Rule 144A under the Securities Act and (b) in offers and sales that occur outside the United States to persons other than U.S. persons (“non-US purchasers,” which term shall include dealers or other professional fiduciaries in the United States acting on a discretionary basis for non-US beneficial owners (other than an estate or trust)), in offshore transactions meeting the requirements of Rule 903 of Regulation S. As used herein, the terms “offshore transactions,” “United States” and “US person” have the respective meanings given to them in Regulation S.

Each purchaser of new notes will be deemed to have represented and agreed with us and the initial purchasers as follows:

- (1) It is purchasing the new notes for its own account or an account with respect to which it exercises sole investment discretion and that it and any such account is (a) a QIB, and is aware that the sale to it is being made in reliance on Rule 144A under the Securities Act or (b) a non-US purchaser that is outside the United States (or a non-US purchaser that is a dealer or other fiduciary as referred to above);
- (2) It understands that the new notes are being offered in a transaction not involving any public offering in the United States within the meaning of the Securities Act, that the new notes have not been and will not be registered under the Securities Act, and that the new notes may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except as set forth below;
- (3) It shall not resell or otherwise transfer any of such new notes prior to (a) the date which is one year (or such other period of time as permitted by Rule 144(d) under the Securities Act or any successor provision thereunder) after the later of the date of original issuance of the new notes and (b) such later date, if any, as may be required by applicable laws except:
  - to the Company or any of its subsidiaries;
  - pursuant to a registration statement which has been declared effective under the Securities Act;
  - within the United States to a QIB in compliance with Rule 144A under the Securities Act;
  - outside the United States to non-US purchasers in offshore transactions meeting the requirements of Rule 904 of Regulation S under the Securities Act; or
  - pursuant to another available exemption from the registration requirements of the Securities Act;
- (4) It agrees that it will give notice of any restrictions on transfer of such new notes to each person to whom it transfers the new notes;
- (5) It understands that the certificates evidencing the new notes (other than the Regulation S Global Notes) will bear a legend substantially to the following effect unless otherwise agreed by us and the trustee:

UNLESS THIS CERTIFICATE IS PRESENTED BY AN AUTHORIZED REPRESENTATIVE OF THE DEPOSITORY TRUST COMPANY, A NEW YORK CORPORATION (“DTC”), TO THE COMPANY OR ITS AGENT FOR REGISTRATION OF TRANSFER, EXCHANGE, OR PAYMENT, AND ANY CERTIFICATE ISSUED IS REGISTERED IN THE NAME OF CEDE & CO. OR IN SUCH OTHER NAME AS IS REQUESTED BY AN AUTHORIZED REPRESENTATIVE OF DTC (AND ANY PAYMENT IS MADE TO CEDE & CO. OR TO SUCH OTHER ENTITY AS IS REQUESTED BY AN AUTHORIZED REPRESENTATIVE OF DTC), ANY TRANSFER, PLEDGE, OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL INASMUCH AS THE REGISTERED OWNER HEREOF, CEDE & CO., HAS AN INTEREST HEREIN.

THE SECURITIES EVIDENCED HEREBY HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE “SECURITIES ACT”), OR ANY STATE OR OTHER SECURITIES LAWS, AND MAY NOT BE OFFERED, SOLD, PLEDGED, OR OTHERWISE TRANSFERRED EXCEPT IN ACCORDANCE WITH THE FOLLOWING SENTENCE. BY ITS ACQUISITION HEREOF OR OF A BENEFICIAL INTEREST HEREIN, THE HOLDER OF THIS SECURITY BY ITS ACCEPTANCE HEREOF (1) REPRESENTS THAT IT, AND ANY ACCOUNT FOR WHICH IT IS ACTING, (A) IS A “QUALIFIED INSTITUTIONAL BUYER” (WITHIN THE MEANING OF RULE 144A UNDER THE SECURITIES ACT) OR (B) IS NOT A U.S. PERSON AND IS ACQUIRING THIS SECURITY IN AN “OFFSHORE TRANSACTION” PURSUANT TO RULE 903 OR 904 OF REGULATION S AND, WITH RESPECT TO (A) AND (B), EXERCISES SOLE INVESTMENT DISCRETION WITH RESPECT TO SUCH ACCOUNT, (2) AGREES FOR THE BENEFIT OF THE COMPANY THAT IT WILL NOT OFFER, SELL, PLEDGE OR OTHERWISE TRANSFER THIS SECURITY OR ANY BENEFICIAL INTEREST HEREIN PRIOR TO THE RESALE RESTRICTION TERMINATION DATE (AS DEFINED IN THE NEXT PARAGRAPH), EXCEPT (A) (I) TO THE COMPANY OR ANY SUBSIDIARY THEREOF, (II) PURSUANT TO A REGISTRATION STATEMENT THAT HAS BECOME EFFECTIVE UNDER THE SECURITIES ACT, (III) TO A QUALIFIED INSTITUTIONAL BUYER IN COMPLIANCE WITH RULE 144A UNDER THE SECURITIES ACT, (IV) IN AN OFFSHORE TRANSACTION COMPLYING WITH THE REQUIREMENTS OF RULE 903 OR RULE 904 OF REGULATION S UNDER THE SECURITIES ACT, OR (V) PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT PROVIDED BY RULE 144 THEREUNDER (IF AVAILABLE), AND (B) IN ACCORDANCE WITH ALL APPLICABLE SECURITIES LAWS OF THE STATES OF THE UNITED STATES AND OTHER JURISDICTIONS, AND (3) AGREES THAT IT WILL GIVE TO EACH PERSON TO WHOM THIS SECURITY IS TRANSFERRED A NOTICE SUBSTANTIALLY TO THE EFFECT OF THIS LEGEND. AS USED HEREIN, THE TERMS “OFFSHORE TRANSACTION,” “UNITED STATES” AND “US PERSON” HAVE THE RESPECTIVE MEANINGS GIVEN TO THEM BY REGULATION S UNDER THE SECURITIES ACT.

THE RESALE RESTRICTION TERMINATION DATE WILL BE THE DATE:

(1) THAT IS AT LEAST ONE YEAR AFTER THE LAST ORIGINAL ISSUE DATE HEREOF; AND  
(2) ON WHICH THE COMPANY INSTRUCTS THE TRUSTEE THAT THIS LEGEND (OTHER THAN THE FIRST PARAGRAPH HEREOF) SHALL BE DEEMED REMOVED FROM THIS SECURITY, IN ACCORDANCE WITH THE PROCEDURES DESCRIBED IN THE INDENTURE RELATING TO THIS SECURITY.

PRIOR TO THE REGISTRATION OF ANY TRANSFER IN ACCORDANCE WITH PARAGRAPH 2A(V) ABOVE, THE COMPANY AND THE TRUSTEE RESERVE THE RIGHT TO REQUIRE THE DELIVERY OF SUCH LEGAL OPINIONS, CERTIFICATIONS, OR OTHER EVIDENCE AS MAY REASONABLY BE REQUIRED IN ORDER TO DETERMINE THAT THE PROPOSED TRANSFER IS BEING MADE IN COMPLIANCE WITH THE SECURITIES ACT AND APPLICABLE STATE SECURITIES LAWS. NO REPRESENTATION IS MADE AS TO THE AVAILABILITY OF ANY EXEMPTION FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT.<sup>1</sup>

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<sup>1</sup> This legend (other than the first paragraph hereof) shall be deemed removed from the face of this Security without further action of the Company, the Trustee, or the holders of this Security at such time as the Company instructs the Trustee to remove such legend pursuant to the Indenture.



- (6) If it is a non-US purchaser acquiring a beneficial interest in a Regulation S Global Note offered pursuant to this offering circular, it acknowledges and agrees that, until the expiration of the 40 day “distribution compliance period” within the meaning of Regulation S, any offer, sale, pledge or other transfer shall not be made by it in the United States or to, or for the account or benefit of, a U.S. person, except pursuant to Rule 144A to a QIB taking delivery thereof in the form of a beneficial interest in a Rule 144A Global Note, and that each Regulation S Global Note will contain a legend to substantially the following effect:

PRIOR TO EXPIRATION OF THE 40-DAY DISTRIBUTION COMPLIANCE PERIOD (AS DEFINED IN REGULATION S (“REGULATION S”) UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE “SECURITIES ACT”)), THIS SECURITY MAY NOT BE REOFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED WITHIN THE UNITED STATES (AS DEFINED IN REGULATION S) OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, A U.S. PERSON (AS DEFINED IN REGULATION S), EXCEPT TO A QUALIFIED INSTITUTIONAL BUYER IN COMPLIANCE WITH RULE 144A UNDER THE SECURITIES ACT IN A TRANSACTION MEETING THE REQUIREMENTS OF THE INDENTURE REFERRED TO HEREIN.

- (7) It acknowledges that the foregoing restrictions apply to holders of beneficial interests in the new notes, as well as holders of the new notes;
- (8) It acknowledges that the trustee will not be required to accept for registration of transfer any new notes acquired by it, except upon presentation of evidence satisfactory to Axtel and the trustee that the restrictions set forth herein have been complied with; and
- (9) It acknowledges that the Company, the trustee, the initial purchasers and others will rely upon the truth and accuracy of the foregoing acknowledgments, representations and agreements and agrees that if any of the acknowledgments, representations or agreements deemed to have been made by its purchase of the new notes are no longer accurate, it shall promptly notify Axtel, the trustee and the initial purchasers. If it is acquiring the new notes as a fiduciary or agent for one or more investor accounts, it represents that it has sole investment discretion with respect to each such account and it has full power to make the foregoing acknowledgments, representations and agreements on behalf of each such account.

## NOTICE TO CANADIAN INVESTORS

### Resale Restrictions

The distribution of the new notes in Canada is being made only on a private placement basis exempt from the requirement that we prepare and file a prospectus with the securities regulatory authorities in each province where trades of the new notes are made. Any resale of the new notes in Canada must be made under applicable securities laws, which will vary depending on the relevant jurisdiction, and which may require resales to be made under available statutory exemptions or under a discretionary exemption granted by the applicable Canadian securities regulatory authority. Purchasers are advised to seek legal advice prior to any resale of the new notes.

### Representations of Purchasers

By purchasing the new notes in Canada and accepting a purchase confirmation a purchaser is representing to us and the dealer from whom the purchase confirmation is received that:

- the purchaser is entitled under applicable provincial securities laws to purchase the new notes without the benefit of a prospectus qualified under those securities laws,
- where required by law, the purchaser is purchasing as principal and not as agent,
- the purchaser has reviewed the text above under Resale Restrictions, and
- the purchaser acknowledges and consents to the provision of specified information concerning its purchase of the new notes to the regulatory authority that by law is entitled to collect the information.

Further details concerning the legal authority for this information is available on request.

### Rights of Action—Ontario Purchasers Only

Under Ontario securities legislation, certain purchasers who purchase a security offered by this circular during the period of distribution will have a statutory right of action for damages, or while still the owner of the new notes, for rescission against us in the event that this circular contains a misrepresentation without regard to whether the purchaser relied on the misrepresentation. The right of action for damages is exercisable not later than the earlier of 180 days from the date the purchaser first had knowledge of the facts giving rise to the cause of action and three years from the date on which payment is made for the new notes. The right of action for rescission is exercisable not later than 180 days from the date on which payment is made for the new notes. If a purchaser elects to exercise the right of action for rescission, the purchaser will have no right of action for damages against us. In no case will the amount recoverable in any action exceed the price at which the new notes were offered to the purchaser and if the purchaser is shown to have purchased the securities with knowledge of the misrepresentation, we will have no liability. In the case of an action for damages, we will not be liable for all or any portion of the damages that are proven to not represent the depreciation in value of the new notes as a result of the misrepresentation relied upon. These rights are in addition to, and without derogation from, any other rights or remedies available at law to an Ontario purchaser. The foregoing is a summary of the rights available to an Ontario purchaser. Ontario purchasers should refer to the complete text of the relevant statutory provisions.

### Enforcement of Legal Rights

All of our directors and officers as well as the experts named herein may be located outside of Canada and, as a result, it may not be possible for Canadian purchasers to effect service of process within Canada upon us or those persons. All or a substantial portion of our assets and the assets of those persons may be located outside of Canada and, as a result, it may not be possible to satisfy a judgment against us or those persons in Canada or to enforce a judgment obtained in Canadian courts against us or those persons outside of Canada.

## **Taxation and Eligibility for Investment**

Canadian purchasers of the new notes should consult their own legal and tax advisors with respect to the tax consequences of an investment in the new notes in their particular circumstances and about the eligibility of the new notes for investment by the purchaser under relevant Canadian legislation.

## **LEGAL MATTERS**

Cahill Gordon & Reindel LLP will pass upon certain United States legal matters for us in connection with the new notes offered hereby. D&A Morales y Asociados, S.C., Monterrey, Mexico, will pass upon certain Mexican legal matters for us in connection with the new notes offered hereby. The initial purchasers have been represented by Milbank, Tweed, Hadley & McCloy LLP, New York, New York and Creel, García-Cuellar, Aiza y Enríquez, S.C., Mexico City, Mexico.

## **INDEPENDENT AUDITORS**

The consolidated financial statements of Axtel S.A.B. de C.V. and subsidiaries as of December 31, 2009 and 2008, and for each of the years in the three-year period ended December 31, 2009, included in this offering circular have been audited by KPMG Cardenas Dosal, S.C., an independent public accounting firm, as stated in their report appearing herein.

## LISTING AND GENERAL INFORMATION

### Clearing Systems

Application has been made to have the notes accepted for clearance through Euroclear and Clearstream. In addition, application has been made to have the notes accepted for trading in book-entry form by DTC. For the Rule 144A notes, the ISIN number is US05462GAC87 and the CUSIP number is 05462GAC8. For the Regulation S notes, the ISIN number is USP06064AC66 and the CUSIP number is P06064AC6 .

### Listing

Application has been made to the Luxembourg Stock Exchange, for the notes to be traded on the EuroMTF market, a market of the Luxembourg Stock Exchange. Copies of our by-laws, the indenture, as may be amended or supplemented from time to time, our published annual audited consolidated financial statements and any published quarterly unaudited consolidated financial statements will be available at our principal executive offices, as well as at the offices of the trustee, registrar, paying agent and transfer agent, and at the offices of the Luxembourg listing agent, paying agent and transfer agent, as such addresses are set forth in this offering circular. We do not publish unconsolidated financial statements. We believe the auditor's reports included herein have been accurately reproduced. We will maintain a paying and transfer agent in Luxembourg for so long as any of the notes are listed on the Luxembourg Stock Exchange.

The notes have not been and will not be listed in the BMV or registered with the Mexican National Securities Registry and therefore the notes may not be offered or sold publicly, or otherwise be the subject of brokerage activities in Mexico, except pursuant to a private placement exemption set forth under Article 8 of the Mexican Securities Market Law.

### Litigation

We are from time to time involved in certain legal proceedings not described herein that are incidental to the normal conduct of our business. We do not believe that the outcome of any such proceedings, if decided adversely to our interests, will have a material effect on our financial condition, cash flows or results of operations. For a more detailed description of our legal proceedings and the risk factors involved therewith, please refer to the descriptions under the headings "Risk Factors" and "Business—Legal Proceedings" in this offering circular.

**INDEX TO FINANCIAL STATEMENTS**  
**CONSOLIDATED FINANCIAL STATEMENTS**  
**OF AXTEL S.A.B. DE C.V. AND SUBSIDIARIES**

**Consolidated Financial Statements**

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**Independent Auditors' Report**  
**(Translation from Spanish Original)**

The Board of Directors and Stockholders  
Axtel, S.A.B. de C.V.:

We have audited the accompanying consolidated balance sheets of Axtel, S.A.B. de C.V. and subsidiaries (the Company) as of December 31, 2009 and 2008, and the related consolidated statements of operations, changes in stockholders' equity for each of the years in the three-year period ended December 31, 2009, the consolidated statements of cash flows for the years ended December 31, 2009 and 2008, and the consolidated statement of changes in financial position for the year ended December 31, 2007. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

During 2009, accounting changes were made as disclosed in Note 4 to the consolidated financial statements which were recognized retrospectively.

As discussed in note 4 to the consolidated financial statements, on January 1, 2008 the FRS B-2 "Statement of Cash Flows" came into effect superseding Bulletin B-12 "Statement of Changes in Financial Position"; accordingly, as of such date and in a prospective manner, the Company presents the consolidated statement of cash flows; therefore, such statement and the consolidated statement of changes in financial position are not presented for comparison purposes.

As mentioned in notes 21 (a) and 21 (b) the Company has contingencies related to interconnection rates with mobile operators and with long distance terminating calls with Teléfonos de México (Telmex). On December 31, 2009, the differences between the amounts paid by the Company and the amounts billed by the mobile operators and Telmex amounted to approximately Ps. 950 million and Ps. 764 million, respectively, before value added tax. At the date of this report, the Administration of the Company and its legal advisors consider that they have sufficient elements to obtain favorable results in the trials related to such contingencies.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Axtel, S.A.B. de C.V. and its subsidiaries as of December 31, 2009 and 2008, and the consolidated results of their operations, and the changes in their stockholders' equity for each of the years in the three-year period ended December 31, 2009, the consolidated cash flows for the years ended December 31, 2009 and 2008 and the consolidated changes in their financial position for the year ended December 31, 2007, in conformity with Mexican Financial Reporting Standards.

KPMG Cárdenas Dosal, S.C.

Leandro Castillo Parada

Monterrey, N.L., México  
February 16, 2010

**AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**

**Consolidated Balance Sheets  
December 31, 2009 and 2008  
(Thousands of Mexican pesos)**

	2009	2008
<b>Assets</b>		
Current assets:		
Cash and cash equivalents .....	Ps. 1,402,240	1,105,576
Accounts receivable, net (note 6) .....	1,851,688	1,796,664
Refundable taxes and other accounts receivable .....	197,946	250,284
Prepaid expenses .....	33,833	33,104
Inventories (note 9) .....	170,681	138,898
Financial instruments (notes 7a and 7b) .....	574,132	475,730
Total current assets .....	4,230,520	3,800,256
Long-term accounts receivable .....	18,491	20,098
Property, systems and equipment, net (note 10) .....	15,210,619	15,306,448
Intangible assets, net (note 13) .....	582,782	820,319
Pre-operating expenses, net (note 11) .....	34,307	64,120
Deferred income taxes (note 18) .....	1,150,507	1,192,323
Deferred employees' statutory profit sharing (note 18) .....	9,707	7,815
Investment in shares of associated company and other permanent investments (note 12) .....	16,295	18,008
Other assets, net (note 14) .....	349,854	339,774
Total assets .....	Ps.21,603,082	21,569,161
<b>Liabilities and Stockholders' Equity</b>		
Current liabilities:		
Accounts payable and accrued liabilities .....	Ps. 2,052,204	2,590,567
Accrued interest .....	215,538	136,532
Taxes payable .....	108,033	133,985
Current maturities of long-term debt (note 15) .....	944,553	296,106
Other accounts payable (note 16) .....	371,503	358,014
Deferred revenue .....	559,542	547,628
Derivative financial instruments (note 7a) .....	30,941	—
Total current liabilities .....	4,282,314	4,062,832
Long-term debt, excluding current maturities (note 15) .....	8,947,650	9,358,464
Other long-term accounts payable .....	14,438	7,932
Employee benefits (note 17) .....	70,630	63,345
Deferred revenue .....	87,117	145,171
Total liabilities .....	13,402,149	13,637,744
Stockholders' equity (note 19):		
Common stock .....	7,562,075	7,562,075
Additional paid-in capital .....	741,671	741,671
Reserves for own shares .....	162,334	162,334
Deficit .....	(273,926)	(649,779)
Change in the fair value of derivative financial instruments (note 7a) .....	8,779	115,116
Total stockholders' equity .....	8,200,933	7,931,417
Commitments and contingencies (note 21)		
Subsequent events (notes 21(b) and 21(j))		
Total liabilities and stockholders' equity .....	Ps.21,603,082	21,569,161

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

**AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**

**Consolidated Statements of Operations**  
**Years ended December 31, 2009, 2008 and 2007**  
**(Thousands of Mexican pesos)**

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Telephone services and related revenues (note 20) . . . . .	Ps. 10,968,877	11,572,401	12,190,610
Operating costs and expenses:			
Cost of revenues and services . . . . .	(2,987,088)	(3,704,876)	(4,504,713)
Selling and administrative expenses . . . . .	(4,143,209)	(3,657,123)	(3,601,427)
Depreciation and amortization . . . . .	(3,065,798)	(2,855,839)	(2,690,687)
	<u>(10,196,095)</u>	<u>(10,217,838)</u>	<u>(10,796,827)</u>
Operating income . . . . .	<u>772,782</u>	<u>1,354,563</u>	<u>1,393,783</u>
Comprehensive financing result:			
Interest expense (note 15) . . . . .	(925,261)	(801,687)	(869,472)
Interest income . . . . .	24,513	58,938	78,864
Foreign exchange gain (loss), net . . . . .	279,814	(1,602,127)	972
Change in the fair value of financial instruments (notes 7a and 7b) . . . . .	212,262	54,051	19,942
Monetary position gain . . . . .	—	—	268,797
Comprehensive financing result, net . . . . .	<u>(408,672)</u>	<u>(2,290,825)</u>	<u>(500,897)</u>
Employees' statutory profit sharing (note 18) . . . . .	(11,152)	(7,974)	(6,088)
Deferred employees' statutory profit sharing (note 18) . . . . .	1,892	(6,365)	(13,594)
Other income (expenses), net (note 2) . . . . .	10,404	(54,055)	(438)
Other income (expense), net . . . . .	<u>1,144</u>	<u>(68,394)</u>	<u>(20,120)</u>
Income (loss) before income taxes and equity in earnings of associated company . . . . .	365,254	(1,004,656)	872,766
Income taxes (note 18):			
Income tax expense . . . . .	(16,588)	(15,556)	(98,819)
Deferred income tax . . . . .	(119,431)	286,045	(284,381)
Flat tax . . . . .	(74,454)	(962)	—
Deferred flat tax . . . . .	29,052	32,046	—
Total income tax (expense) benefit . . . . .	<u>(181,421)</u>	<u>301,573</u>	<u>(383,200)</u>
Equity in earnings of associated company (note 12) . . . . .	<u>(7,433)</u>	<u>2,759</u>	<u>1,430</u>
Net income (loss) . . . . .	<u>Ps. 176,400</u>	<u>(700,324)</u>	<u>490,996</u>
Weighted average of common shares outstanding . . . . .	<u>8,769,353,223</u>	<u>8,769,353,223</u>	<u>8,754,493,119</u>
Basic and diluted earnings (loss) per share (pesos) (note 19) . . . . .	<u>Ps. 0.02</u>	<u>(0.08)</u>	<u>0.06</u>

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

**AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**

**Consolidated Statements of Cash Flows**  
**Years ended December 31, 2009 and 2008**  
**(Thousands of Mexican pesos)**

	<b>2009</b>	<b>2008</b>
Operating activities:		
Net income (loss) .....	Ps. 176,400	(700,324)
Income taxes .....	181,421	(301,573)
Employees' statutory profit sharing .....	9,260	14,339
Items related with investing activities:		
Depreciation .....	2,777,495	2,524,668
Amortization .....	288,303	331,171
Loss (gain) in sale of property, system and equipment .....	16,599	(569)
Equity in earnings of associated company .....	7,433	(2,759)
Items related with financing activities:		
Interest expense .....	925,261	801,687
Amortization of premium on bond issuance .....	(3,571)	(4,549)
Cancellation of intangible assets .....	16,367	—
Change in the fair value of derivative financial instruments .....	(212,262)	(54,051)
Subtotal .....	4,182,706	2,608,040
Increase in accounts receivable .....	(259,872)	(33,017)
Increase in allowance for doubtful accounts .....	204,847	58,702
(Increase) decrease in inventories .....	(31,783)	28,992
Decrease (increase) in other accounts receivable .....	6,618	(121,483)
(Decrease) increase in accounts payable .....	(554,780)	651,408
Taxes paid .....	(62,716)	(150,504)
Decrease in deferred revenue .....	(46,140)	(93,479)
Increase (decrease) in other accounts payable and other liabilities .....	10,640	(107,721)
Net cash flow from operating activities .....	3,449,520	2,840,938
Investing activities:		
Acquisition and construction of property, systems and equipment, net .....	(2,674,436)	(4,000,615)
Increase in financial instruments and other investments .....	(229,090)	—
Other assets .....	(100,513)	(19,267)
Net cash flow from investing activities .....	(3,004,039)	(4,019,882)
Cash surplus to be applied in (cash to be obtained from) financing activities .....	445,481	(1,178,944)
Financing activities:		
Own shares sold .....	219,662	—
Own shares acquired .....	—	(277,666)
Interest paid .....	(848,240)	(715,161)
Long terms loans, net .....	777,967	215,842
Change in the fair value of derivative financial instruments .....	(18,392)	(114,499)
Net cash flow from financing activities .....	130,997	(891,484)
Net increase (decrease) in cash and cash equivalents .....	576,478	(2,070,428)
Adjustment to cash flow from changes in foreign exchange .....	(279,814)	1,602,127
Cash and cash equivalents at beginning of year .....	1,105,576	1,573,877
Cash and cash equivalents at the end of year .....	Ps. 1,402,240	1,105,576

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

**AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**  
**Consolidated Statement of Changes in Financial Position**  
**For the year ended December 31, 2007**  
**(Thousands of Mexican pesos)**

Operating activities:	
Net income .....	Ps. 490,996
Add charges (deduct credits) to operations not requiring (providing) resources:	
Depreciation .....	2,299,574
Amortization .....	391,113
Accrual for seniority premiums and severance payments .....	11,324
Deferred income tax and employee's profit sharing .....	297,975
Equity in earnings of associated company .....	(1,430)
Resources provided by operations .....	3,489,552
Investment in operations .....	(262,804)
Resources provided by operating activities .....	<u>3,226,748</u>
Financing activities:	
Increase in common stock .....	192,280
Additional paid-in capital .....	194,540
Payments on loans, net .....	(812,371)
Accrued interest .....	95,403
Other accounts payable .....	11,523
Resources used by financing activities .....	<u>(318,625)</u>
Investing activities:	
Acquisition and construction of property, systems and equipment, net .....	(2,486,093)
Other assets .....	(70,298)
Resources used in investing activities .....	<u>(2,556,391)</u>
Increase in cash and cash equivalents .....	351,732
Cash and cash equivalents at beginning of year .....	<u>1,222,145</u>
Cash and cash equivalents at end of year .....	<u>Ps. 1,573,877</u>

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

**AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**  
**Consolidated Statements of Changes in Stockholders' Equity**  
**For the years ended December 31, 2009, 2008 and 2007**  
**(Thousands of Mexican pesos)**

	Common stock	Additional paid-in capital	Reserves for own shares	(Deficit)	Cumulative deferred income tax effect	Change in the fair value of derivative instruments	Total stockholders' equity
Balances as of December 31, 2006 .....	Ps.8,677,782	547,131	—	(1,440,606)	132,168	(32,153)	7,884,322
Issuance of common stock (note 19a) .....	192,280	194,540	—	—	—	—	386,820
Comprehensive income (note 19c) .....	—	—	—	490,996	—	(11,792)	479,204
Balances as of December 31, 2007 .....	Ps.8,870,062	741,671	—	(949,610)	132,168	(43,945)	8,750,346
Effects of the application of FRS D-4 (note 3q) .....	—	—	—	132,168	(132,168)	—	—
Absorption of accumulated deficit from prior years (note 19a) .....	(1,307,987)	—	—	1,307,987	—	—	—
Reserves for own shares (note 19a) .....	—	—	440,000	(440,000)	—	—	—
Own shares acquired (note 19a) .....	—	—	(277,666)	—	—	—	(277,666)
Comprehensive loss (note 19c) .....	—	—	—	(700,324)	—	159,061	(541,263)
Balances as of December 31, 2008 .....	7,562,075	741,671	162,334	(649,779)	—	115,116	7,931,417
Effects of the application of FRS C-8 (notes 4d and 11) .....	—	—	—	(20,209)	—	—	(20,209)
Own shares sold (note 19a) .....	—	—	—	219,662	—	—	219,662
Comprehensive income (note 19c) .....	—	—	—	176,400	—	(106,337)	70,063
Balances as of December 31, 2009 .....	Ps.7,562,075	741,671	162,334	(273,926)	—	8,779	8,200,933

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



## **AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**

### **Notes to the Consolidated Financial Statements December 31, 2009, 2008 and 2007 (Thousands of Mexican pesos)**

#### **(1) Authorization and basis of presentation**

These financial statements have been translated from the Spanish language original and for the convenience of the English-speaking readers.

On February 16, 2010, the Administration of the Company authorized the issuance of the accompanying consolidated financial statements and related notes thereto.

According to Mexican General Corporation Law and the bylaws of the Company, the stockholders are empowered to modify the financial statements after their issuance. The accompanying financial statements will be submitted to the next Stockholders' Meeting for approval.

The accompanying consolidated financial statements have been prepared in accordance with Mexican Financial Reporting Standards (FRS) in effect as of the balance sheet date.

#### **(2) Description of business and significant transactions**

Axtel, S.A.B. de C.V. and subsidiaries (the Company or AXTEL) is a Mexican corporation engaged in operating and/or exploiting a public telecommunication network to provide voice, sound, data, text, and image conducting services, and local, national, and international long-distance calls. To provide these services and carry out the Company's activity, a concession is required (see notes 21 (f) and (g)). In June 1996, the Company obtained a concession from the Mexican Federal Government to install, operate and exploit public telecommunication networks for an initial period of thirty years.

AXTEL offers different access technologies, including fixed wireless access, point-to-point, point-to-multipoint radio links, WiMAX, fiber optic and copper technology, which are used depending on the communication needs of the clients.

On September 22, 2009, the Company completed an issuance of senior unsecured notes, for an amount of U.S. \$300 million with due date September 22, 2019 and with an annual interest rate of 9.0% which will be paid semiannually starting March 22, 2010. The proceeds of this issuance were used to reduce outstanding debt as described in note 15.

In order to implement its strategic plans, the Company restructured some of its operations during the year ended December 31, 2008 in some of its operational areas. The cost of this restructuring, consisting of compensation and employee severance payments amounted to Ps. 39,354, and is included in the statement of operations for the year ended December 31, 2008 as part of the other expenses.

As described in note 19, during July 2008, the Company began a share buyback program which was approved at an ordinary shareholders' meeting held on April 23, 2008 for up to Ps. 440 million. During 2009 the totality of shares repurchased were sold again in the market.

In an ordinary shareholders' meeting held on July 15, 2008, the stockholders approved the merger of Impulsora e Inmobiliaria Regional, S.A. de C.V., Adequip, S.A. de C.V., Avantel Equipos, S.A. de C.V., Avantel Recursos, S.A. de C.V., Avantel Servicios, S.A. de C.V. and Avantel Telecomunicaciones, S.A. de C.V. (as the mergers companies) with Servicios Axtel, S. A. de C. V. (as the merging company). The merger was effective among the parties and in relation with third parties since August 1, 2008 and doesn't have any impact on the operation or the consolidated figures of the Company.

**AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**  
**Notes to the Consolidated Financial Statements—(Continued)**  
**December 31, 2009, 2008 and 2007**  
**(Thousands of Mexican pesos)**

**(3) Summary of significant accounting policies**

The accounting policies and practices followed by the Company in the preparation of the consolidated financial statements are described below:

*(a) Use of estimates*

The preparation of consolidated financial statements in conformity with financial reporting standards requires management of the Company to make a number of estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying amount of property, systems and equipment, valuation allowances for receivables, inventories and deferred income tax assets; valuation of derivative instruments; and assets and obligations related to employee benefits. Due to current economic environment, actual results could differ from those estimates and assumptions. Those estimates are based on the better judgment of the management of the Company. Company's management evaluates its estimated and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment which management believes to be reasonable under the circumstances. Management adjusts the assumptions when facts and circumstances dictate.

For purposes of disclosure in the notes to the consolidated financial statements, references to pesos or "Ps.," are to Mexican pesos; likewise, references to dollars or U.S. \$, or USD are to dollars of the United States of America.

*(b) Recognition of the effects of inflation*

The accompanying consolidated financial statements have been prepared in accordance with financial reporting standards (FRS) in effect as of the balance sheet date and include the recognition of the effects of inflation on the financial information through December 31, 2007, based upon the Mexican National Consumer Price Index (NCPI) published by Banco de México. Cumulative inflation percentage of the three preceding years and the indexes used to recognized inflation through such year were as follows:

<u>December 31,</u>	<u>NCPI</u>	<u>Inflation</u>	
		<u>Yearly</u>	<u>Cumulative</u>
2009 .....	138.541	3.57%	14.48%
2008 .....	133.761	6.53%	15.01%
2007 .....	125.564	3.76%	11.56%

*(c) Principles of consolidation*

The consolidated financial statements include the financial statements of Axtel and its subsidiaries. All significant balances and intercompany transactions have been eliminated in the preparation of the consolidated financial statements. The consolidation was made based on audited financial statements of each of the subsidiaries as of December 31, 2009 and 2008, which were prepared in accordance with the FRS.

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The Company owns directly or indirectly 100% of the following subsidiaries:

	<b>Main activity</b>
Instalaciones y Contrataciones, S. A. de C. V. (“Icosa”) . . . . .	Administrative services
Servicios Axtel, S. A. de C. V. (“Servicios Axtel”) . . . . .	Administrative services
Avantel, S. de R.L. de C.V. (“Avantel”)* . . . . .	Telecommunication services
Avantel Infraestructura S. de R.L. de C.V. (“Avantel Infraestructura”)* . . . . .	Telecommunications services
Telecom. Network, Inc. (“Telecom”) . . . . .	Telecommunications services

\* On June 30, 2005, Avantel Infraestructura and certain subsidiaries as partners, together with Avantel as a representative partner of the Joint Venture, entered into a Joint Venture agreement to permit Avantel provide services and operate Avantel Infraestructura’s public telecommunications network. Under this agreement, Avantel Infraestructura contributed the concessioned network, and the other associates contributed the customer agreements, as well as support and human resources services.

As a result of the above, Avantel Infraestructura entered into an agreement with Avantel to transfer the concession rights granted by the Secretaria de Comunicaciones y Transportes (“SCT”).

***(d) Cash equivalents***

Cash equivalents of Ps. 1,335,670 and Ps. 989,494 at December 31, 2009 and 2008, respectively, consist of overnight repurchase agreements and certificates of deposit with an initial term of less than three months. Cash equivalents are carried at the lower of acquisition cost plus accrued interest as of the most recent balance sheet date or net estimated realizable value. Interest and foreign currency exchange fluctuation are included in the statements of operations as part of the comprehensive financing result.

***(e) Trade accounts receivable***

Trade accounts receivable includes the amount billed to customers and a provision for services rendered at the balance sheet date but not billed. Amounts billed are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is the Company’s best estimate of the amount of probable credit losses in the Company’s existing accounts receivable. The Company reviews its allowance for doubtful accounts monthly. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential recovery is considered remote.

***(f) Investment in shares of associated company and other permanent investments***

The investment in shares of associated company is accounted for by the equity method. The other permanent investments are recorded at the acquisition cost.

***(g) Inventories and cost of sales***

Inventories are carried at the lower of cost or net realizable value. Cost of revenues include expenses related to the termination of customers’ cellular and long-distance calls in other carriers’ networks, as well as expenses related to billing, payment processing, operator services and our leasing of private circuit links.

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***(h) Property, systems and equipment***

Property, system and equipment, including capital leases, are initially recorded at acquisition cost and until December 31, 2007, adjusted for inflation by using factors derived from the NCPI.

Starting January 1, 2007, the acquisitions of assets in period of construction or installation include the corresponding comprehensive financing result as part of the assets value.

Depreciation of property, systems and equipment is calculated using the straight-line method, based on useful lives estimated by management. Useful lives are described in note 10.

Leasehold improvements are amortized over the useful life of the improvement or the related contract term, whichever is shorter.

Maintenance and repairs, including the cost of replacing minor items not constituting substantial improvements are expensed as incurred and charged principally to selling and administrative expenses.

***(i) Telephone concession rights***

Telephone concession rights that are included within intangible assets were restated by NCPI factors until December 31, 2007 and are amortized under the straight-line method over a period of 20 to 30 years (the initial term of the concession rights).

***(j) Pre-operating expenses***

Pre-operating expenses include administrative services, technological advice and comprehensive financing results incurred through June 1999 and also the expenses incurred during 2000, 2004, 2005 and 2006 in opening offices in cities throughout the country. These expenses were capitalized, and until December 31, 2007 were adjusted for inflation based on factors derived from the NCPI and are amortized under the straight-line method over a period of 10 years (see note 11).

***(k) Other and intangible assets***

Other assets mainly include costs related to Telmex / Telnor infrastructure costs, guarantee deposits and notes issuance costs (see note 14).

As a consequence of the acquisition of Avantel and based upon calculations prepared by an independent expert appraiser, the Company recognized certain intangible assets as follows: trade name, customer relationships and concession rights (see note 13).

***(l) Employee benefits***

Termination benefits for reasons other than restructuring and retirement to which employees are entitled are charged to operations for each year, based on actuarial computations using the projected unit credit method. As of December 31, 2009 and for purposes of recognizing benefits upon retirement, the remaining average service life of employees entitled to plan benefits approximates 20.5 years.

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The actuarial gain or loss is recognized directly in the results of the period as is accrued, in the case of termination benefits, and its amortized based in the remaining service life of the employees, for the retirements benefits.

***(m) Derivative financial instruments***

The Company accounts for derivatives and hedging activities in accordance with FRS C-10, which requires that all derivative instruments be recorded on the balance sheet date at their respective fair values.

The Company uses derivative financial instruments in order to manage financial exposures, especially risks associated with foreign currency and interest rates. In accordance with FRS C-10, the Company may apply hedge accounting to such instruments if it meets certain requirements and assesses whether the derivatives that are used in hedging transactions are highly effective in offsetting cash flows of hedged items. The Company accounts for the derivative financial instruments designated as hedging activities into two main classifications: (i) Fair value hedging and (ii) Cash flows hedging.

In addition, the Company has accounted for certain derivative financial instruments under the classification of trade, that did not meet the requirements for hedge accounting at fair value in the balance sheet with changes in fair value recognized directly in the income statement, even though these instruments are highly effective. These derivative instruments expired on December 15, 2008.

The Company uses financial derivative instruments that are designated as a Fair Value Hedge where the gain or loss on a derivative instrument designated and qualifying as a fair value hedging instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk shall be recognized currently in earnings in the same accounting period. For financial derivative instruments designated as a Cash Flow Hedge the effective portion of the gain or loss on a derivative instrument designated and qualifying as a cash flow hedging instrument shall be reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged forecasted transaction affects earnings. The ineffectiveness of a gain or loss on the derivative instrument, if any, shall be recognized currently in earnings.

The ineffectiveness portion of the change in the fair value of a derivative instrument that qualifies as a hedging activity is reported in the income statement.

The Company will discontinue hedge accounting prospectively when it is determined that the derivative is no longer effective in offsetting changes in the fair value or cash flows of the hedged item, the derivative expires or is sold, terminated, or exercised. In all situations in which hedge accounting is discontinued, the Company continues to carry the derivative at its fair value on the balance sheet and recognizes any subsequent changes in the fair value of the financial instrument directly in the income statement. (See note 7a).

***(n) Income taxes (IT), Assets Tax (AT), Flat Rate Business Tax (IETU) and employee statutory profit sharing (ESPS)***

Current IT, IETU and ESPS payable for the year are determined in conformity with the tax provisions in effect.

Deferred IT and from January 1, 2008 deferred IETU and ESPS' are accounted under the asset and liability method. Deferred tax and ESPS assets and liabilities are recognized for the future tax consequences attributable

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to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and in the case of income taxes, for operating loss and asset tax (AT) carryforwards. Deferred tax and ESPS assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax and ESPS assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Until December 31, 2007, deferred ESPS was recognized only for timing differences arising from the reconciliation of book income to income for profit sharing purposes, for which it was reasonably estimated that a future liability or benefit would arise and there was no indication that the liabilities or benefits would not materialize.

***(o) Inflation adjustment of capital stock, other stockholders contributions and deficit***

Until December 31, 2007, the inflation adjustment of capital stock, other stockholders contributions and deficit, was determined by multiplying stockholder contributions and deficit by factors derived from the NCPI, which measure accumulated inflation from the dates such contributions were made or such deficit arose through year end 2007, date on which change was effected to a non-inflationary economy in accordance with FRS B-10 “Effects of Inflation”. The resulting amounts thus obtained represented the constant value of stockholders’ equity.

***(p) Comprehensive income (loss)***

The comprehensive income (loss) represents the net income or loss for the year plus the effect of those items reflected directly in stockholders’ equity, other than capital contributions, reductions and distributions.

***(q) Cumulative deferred income tax effect***

Through December 31, 2007, cumulative deferred income taxes, represented the cumulative effect of the adoption of the deferred taxes accounting standard. In 2008, such amount, for a total of 132,168, was reclassified to deficit.

***(r) Comprehensive financing result (CFR)***

The CFR includes interest income and expense, foreign exchange gain and loss and valuation effects of financial instruments, less the amounts capitalized, as part of fixed assets.

Foreign currency transactions are recorded at the rate of exchange prevailing on the date of execution or settlement. Foreign currency assets and liabilities are translated at the exchange rate in force at the balance sheet date. Exchange differences arising from assets and liabilities denominated in foreign currencies are recognized in the results of operations.

Until December 31, 2007 monetary position gains and losses are determined by multiplying the difference between monetary assets and liabilities at the beginning of each month, including the deferred taxes, by inflation factors through year-end. The aggregate of these results represents the monetary gain or loss for the year arising from inflation, which is recognized in the CFR.



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***(s) Revenue recognition***

The Company's revenues are recognized when earned, as follows:

- *Telephony Services*—The Company generates revenue by enabling customers to originate and receive an unlimited number of calls. Customers are charged a flat monthly fee for basic service, a per call fee for local calls (“measured service”), a per minute usage fee for calls completed on a cellular line (“calling party pays” or “CPP calls”) and national and international long distance calls, and a monthly fee for value-added services and internet services when requested by the customer.
- *Activation*—At the moment of installing the service when the customer has a contract with indefinite life; otherwise is recognized according to the length of the contract between the customer and the Company.
- *Equipment*—At the moment of selling the equipment and when the customer acquires the property of the equipment and assumed all risks.
- *Integrated services*—At the moment when the client receives the service.

***(t) Business risk concentration***

The Company rendered services to three clients that represented approximately 22%, 23% and 21% of total net rental, installation, service and other revenues during 2009, 2008 and 2007. The Company provides an allowance for doubtful accounts based on management's analyses and estimations. The allowance expense is included as selling and administrative expenses in the consolidated statement of operations.

***(u) Contingencies***

Liabilities for loss contingencies are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. When a reasonable estimation can not be made, qualitative disclosure is provided in the notes to the consolidated financial statements. Contingent revenues, earnings or assets are not recognized until their realization is virtually assured.

***(v) Impairment of property, systems and equipment and other non-current assets***

The Company evaluates, at least once a year, the adjusted values of its property, systems and equipment and other non-current assets subject to amortization to determine whether there is an indication of potential impairment or 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 estimated undiscounted cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed off are separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated.

***(w) Segment information***

The Company believes that it operates in one business segment. Management does view the business as consisting of two revenues streams (Mass Market and Business Market); however it is not possible to attribute direct or indirect costs to the individual streams other than selling expenses.

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**(x) Accruals**

The company recognizes, based on the administration estimates, accrual liabilities for those present obligations in which the assets transfer or rendering of services is virtually unavoidable and comes as a consequence of events in the past, mainly interests, salaries and other payments to employees.

**(y) Advertising expenses**

Advertising costs are expensed as incurred.

**(4) Accounting changes**

The Mexican Board of Research and Development of Financial Reporting Standards (Consejo Mexicano para la Investigación y Desarrollo de Normas de Información Financiera or CINIF) has issued the following FRS, effective for years beginning on and after January 1, 2009, with the respective prospective or retrospective application being specified in each case.

- (a) FRS B-7 “Business combinations”**—FRS supersedes Bulletin B-7 and establishes, among other things, general rules for the initial valuation and recognition at the acquisition date of net assets, regarding that all business combinations should be accounted for using the purchase method. The provisions of this FRS became effective for acquisitions effected on or after January 1, 2009. Any accounting change resulting from this FRS is to be applied on a prospective basis.

The application of this FRS did not result in accounting changes to the consolidated financial statements of the Company.

- (b) FRS B-8 “Consolidated or combined financial statements”**—FRS B-8 supersedes Bulletin B-8 “Consolidated and combined financial statements and valuation of investments in shares” and establishes general rules for the preparation and presentation of consolidated and combined financial statements, and related disclosures. Amendments include:

- (i) Required of consolidation of special purpose entities (SPEs) when controlled.
- (ii) The possibility, under certain conditions, of presenting unconsolidated financial statements.
- (iii) Consideration is given to the existence of potential voting rights that might be exercised or converted in favor of the entity in its capacity as holding Company and that may change its interference in decision-making at the time of assessing the existence of control.

The application of this FRS did not result in accounting changes to the consolidated financial statements of the Company.

- (c) FRS C-7 “Investments in associates and other investments”**—FRS C-7 sets forth the rules to account for investments in associates as well as other investments where control, joint control or significant influence is not exercised. The principal changes with respect to the former standard include the following:

- (i) The equity method of accounting is required for SPEs where significant influence is exercised.
- (ii) Consideration is given to the existence of potential voting rights that might be exercised or converted in favor of the entity in its capacity as the holding Company and that may change its interference in decision-making at the time of assessing the existence of significant influence.

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(iii) A specific procedure and a limit for recognition of an associated entity's losses are provided.

The application of this FRS did not result in accounting changes to the consolidated financial statements of the Company.

- (d) **FRS C-8 “Intangible assets”**—FRS C-8 supersedes Bulletin C-8 “**Intangible Assets**” and establishes, among other things, primarily the following revisions:
- (i) Redefinition of intangible assets, establishing that separability is not the only condition for the intangible asset to be identifiable.
  - (ii) The acquisition cost must be considered for the initial valuation, identifying whether it is an individual acquisition, business combination or it is internally generated. Additionally, future financial benefits should be generated.
  - (iii) Subsequent outlays for research and developments in progress should be recorded as expenses if they are part of the research phase or recorded as an intangible asset if they meet the criteria to be recognized as such.
  - (iv) The presumption that the useful life of an intangible asset may not exceed twenty years was eliminated.

As a consequence of the adoption of this FRS, in 2009, the Company canceled the unamortized balance at December 31, 2008 of the pre-operating capitalized costs until December 31, 2002 for an amount of Ps. 19,436, net of deferred income taxes for an amount of Ps. 7,558, against deficit without restating of the financial statements of previous years. In addition the Company Conectividad Inalambrica 7 GHz, S.de R.L., recognized using the equity method, cancelled Ps. 1,546, net of deferred income taxes for an amount of Ps. 312.

In addition, the following FRS were effective for years beginning on or after January 1, 2008:

- (e) **FRS B-10 “Effects of inflation”**—FRS B-10 supersedes Bulletin B-10 “**Recognition of the effects of inflation on the financial information**” and its five amendment documents, as well as the related circulars and Interpretation of Financial Reporting Standards (IFRS) 2. The principal considerations established by this FRS are:
- (i) Recognition of the effects of inflation – An entity operates in a) an inflationary economic environment when cumulative inflation over the immediately preceding 3-year period is equal to or greater than 26%; and b) non-inflationary economic environment, when inflation over the aforementioned period is less than 26%.

For case a), the comprehensive recognition of the effects of inflation is required, (similarly to Bulletin B-10 being superseded). For case b), the effects of inflation are not recognized; however, at the effective date of this FRS and when an entity ceases to operate in an inflationary economic environment, the restatement effects determined through the last period in which the entity operated in an inflationary economic environment (in this case 2008), must be kept and shall be reclassified on the same date and using the same procedure as that of the corresponding assets, liabilities and stockholders' equity. Should the entity once more operate in an inflationary economic environment, the cumulative effects of inflation not recognized in the periods where the environment was deemed as non-inflationary should be recognized retrospectively.

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- (ii) Price index—the use of the National Consumer Price Index (NCPI) or the change in the value of the Investment Unit (UDI) may be used for determining the inflation for a given period.
- (iii) Valuation of inventories and of foreign machinery and equipment—The possibility of using replacement costs for inventories and specific indexation for foreign machinery and equipment is no longer allowed.
- (iv) Equity adjustment for non-monetary Assets—On the effective date of this FRS, the unrealized portion of the equity adjustment for non monetary assets, which is maintained in stockholders' equity, should be identified to be reclassified to earnings of the year when the originating item is realized. The realized portion or when is not practical to identify the unrealized portion, the realized and unrealized portions should be reclassified to retained earnings.
- (v) Monetary Position Gains or Losses (included in Deficit/Excess in Equity Restatement) will be reclassified to retained earnings on the effective date of this FRS.

As a result of the adoption of this FRS, at January 1, 2008 the stockholders' equity accounts were reclassified as shown on the statement of changes in stockholders' equity.

The 2007 consolidated financial statements are presented expressed in constant pesos at December 31, 2007 purchasing power, date on which the comprehensive method for recognizing the effects of inflation was last used.

- (f) **FRS D-3 “Employee benefits”**—FRS D-3 supersedes Bulletin D-3 “*Labor Obligations*”, the sections applicable to Employee Statutory Profit Sharing (ESPS) of Bulletin D-4 and IFRS 4. The principal considerations established by this FRS are:
  - (i) Elimination of the recognition of an additional liability and the related intangible asset or any comprehensive item as a separate element of stockholders' equity.
  - (ii) Employee benefits are classified in four principal categories; direct short-term and long term, termination and post-employment benefits. FRS D-3 establishes a maximum five-year period for amortizing unrecognized/unamortized items while actuarial gains or losses may be recognized as earned or incurred. Unlike termination benefits, post-employment benefits actuarial gains or losses may be immediately recognized in results of operations or amortized over the expected service life of the employees.
  - (iii) The use of nominal rates and the incorporation of the term salary increases due to promotions.
  - (iv) ESPS, including deferred ESPS, shall be presented in the statement of income as ordinary operations, preferably within “other income and expenses”. Furthermore, FRS D-3 establishes that the asset and liability method should be used for determining deferred ESPS; any effects arising from the change in method shall be recognized in retained earnings, without restatement of prior years' financial statements.

As a result from the adoption of this FRS, in 2008 the intangible asset of Ps. 71 reflected in the balance sheet as of December 31, 2007 was eliminated.

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- (g) *FRS D-4 “Taxes on income”*—FRS D-4 supersedes Bulletin D-4 “*Accounting for income and asset taxes and employee statutory profit sharing*” and *Circulars 53 and 54*. The principal considerations established by this FRS are:
- (i) The balance of the cumulative IT effects resulting from the initial adoption of Bulletin D-4 in 2000 is reclassified to retained earnings, unless identified with any other comprehensive item pending reclassification. On January 1, 2008 Ps. 132,168 were reclassified to retained earnings.
  - (ii) The accounting treatment of ESPS (current and deferred) is transferred to FRS D-3, as mentioned in paragraph (b) above.
- (h) *FRS B-2 “Statement of cash flows”*—FRS B-2 supersedes Bulletin B-12 “*Statement of changes in financial position*” and paragraph 33 of Bulletin B-16. The principal considerations established by this FRS are:
- (i) Instead of the statement of changes in financial position, the financial statements shall include the statements of cash flows for all the periods presented comparatively with those of the current year, except for financial statements of periods prior to 2008.
  - (ii) Cash inflows and cash outflows are reported in nominal currency units, thus not including the effects of inflation.
  - (iii) Two alternative preparation methods (direct and indirect) are established, without stating preference for either method. Furthermore, cash flows from operating activities are to be reported first, followed by cash flows from investing activities and lastly by cash flows from financing activities.
  - (iv) Captions of principal items are to be reported gross, with certain exceptions and require disclosure of the composition of items considered cash equivalents.

Accordingly, the Company presents the consolidated statement of changes in financial position for 2007 as issued and the consolidated statements of cash flows for 2009 and 2008 under the indirect method.

**(5) Foreign currency exposure**

Monetary assets and liabilities denominated in dollars as of December 31, 2009 and 2008 are as follows:

	<b>(Thousands of dollars)</b>	
	<b>2009</b>	<b>2008</b>
Current assets . . . . .	94,360	76,762
Current liabilities . . . . .	(138,535)	(126,564)
Long-term liabilities . . . . .	(617,908)	(571,209)
Foreign currency liability position, net. . . . .	<u>(662,083)</u>	<u>(621,011)</u>

The U.S. dollar exchange rates as of December 31, 2009 and 2008 were Ps. 13.05 and Ps. 13.53, respectively. As of February 16, 2010, the exchange rate was Ps. 12.98.

As of December 31, 2009, the Company had foreign exchange derivative instruments (see note 7).

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Following is a summary for the years ended December 31, 2009, 2008 and 2007, of transactions carried out with foreign entities, excluding imports and exports of systems and equipment:

	(Thousands of dollars)		
	2009	2008	2007
Interest expense .....	58,863	57,636	61,493
Commissions .....	412	50	6
Administrative and technical advisory services .....	4,094	6,240	4,107
Cost of services .....	7,526	12,435	1,115
	<u>70,895</u>	<u>76,361</u>	<u>66,721</u>

**(6) Accounts receivable**

Accounts receivable consist of the following:

	2009	2008
Trade .....	Ps.3,509,743	3,249,872
Less allowance for doubtful accounts .....	1,658,055	1,453,208
Accounts receivable, net .....	<u>Ps.1,851,688</u>	<u>1,796,664</u>

The activity in the allowance for doubtful accounts for the years ended December 31, 2009, 2008 and 2007 was as follows:

	2009	2008	2007
Balances at beginning of year .....	Ps.1,453,208	1,394,506	1,204,472
Bad debt expense .....	204,847	193,800	190,034
Adjustment to bad debt expense from previous years .....	—	(135,098)	—
Balances at year end .....	<u>Ps.1,658,055</u>	<u>1,453,208</u>	<u>1,394,506</u>

**(7) Financial instruments**

**(a) Derivative Financial instruments**

The Company and its subsidiaries are exposed, by their normal business relations, to some financial risks denominated as interest rate risk and currency exchange rate risk, principally. To mitigate the exposure to those risks the Company and its subsidiaries use derivative financial instruments.

By using derivative financial instruments to hedge exposures to changes in currency exchange rates fluctuations, the Company exposes itself to credit risk and market risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes the Company, which creates credit counterparty risk for the Company. When the fair value of a derivative contract is negative, the Company owes the counterparty and, therefore, it does not possess credit risk. The Company minimizes the credit risk in derivative instruments by entering into transactions with high-quality foreign financial counterparties.



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For derivative financial instruments that are designated as hedging activities, the Company and its subsidiaries formally document the hedging relationship and its risk management objective and strategy for undertaking the hedge, the hedging instrument, the hedged item, the nature of the risk being hedged, how the hedging instrument's effectiveness in offsetting the hedged risk will be assessed and the methodology to measure the ineffectiveness.

The Company and its subsidiaries undertake prospective and retrospective tests of effectiveness to ascertain in every moment whether the hedging employed remains effective according to applicable accounting standards. At the moment that ineffectiveness is detected, the Company registers that amount in the results as part of the CFR. Due to the fact that the fair value of derivative financial instruments may suffer significant fluctuations, it is very probable that the Company will be exposed to the volatility related to unrealized profits and losses due to the changes in the fair value of derivative financial instruments in the future.

***Derivative financial instruments with hedging purposes***

According to the accounting models for hedging activities that are permitted by financial accounting standards, the dimension, risks and estimated impact in the balance sheet or income statement of the following derivative financial instruments are presented below. In contrast to financial instruments with trading purposes, the derivatives designated as hedges do not generate volatility in the income statement, as long as the instruments are highly effective and continue to meet the financial accounting standards to keep the classification as hedging activities:

*Fair value hedge*

- i) On March 22, 2007, the Company contracted a CCS (Currency Swap) to cover the risk of interest rate and exchange rate generated by the syndicated term loan for U.S. \$110.2 million, which matures in February 2012, in which the Company will receive payments of 3 months Libor plus 150 basis points over U.S. \$110.2 million notional and will pay a monthly rate of TIEE 28 days plus 135 basis points over Ps. 1,215.5 notional which includes the amortizations of principal. This transaction for its characteristics, is registered under the fair value hedge accounting model. During the month of September 2009 the Company prepaid U.S. \$85 million of the portion in U.S. dollars of the syndicated loan, the respective hedge was canceled, and the fair value of such positions was used in new financial instrument that it is mentioned in the following paragraphs. The CCS information is as follows:

(Amounts in charts are expressed in millions)

Counterpart	Notional	Conditions	Estimated fair value (USD)	
			2009	2008
Credit Suisse	Ps. 278 MXP \$25.2 USD	The Company pays TIEE + 135 basis points and receives Libor + 150 basis points	\$3.9	\$23.3

For the year ended December 31, 2009 the change in the fair value of the hedging activity of the syndicated term loan resulted in an unrealized loss amount of U.S. \$7.0 million recognized in the comprehensive financial result, offset it by the change in the fair value of the debt valued at December 31, 2009 in U.S. \$16.1 million.

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*Cash flow hedge*

- i) On March 29, 2004, the Company entered into a derivative a Ps-USD CCS to hedge a portion of its U.S. dollar foreign exchange exposure resulting from the issuance of the U.S. \$175 million. This swap was made to cover 65% of the debt. Under this CCS transactions, Axtel will receive semiannual payments calculated based on the aggregate notional amount of U.S. \$113.75 million at an annual U.S. rate of 11%, and the Company will make semiannual payments calculated based on the aggregate of Ps.1,270.0 (nominal value) at annual rate of 12.30%. This derivative instrument expired on December 15, 2008.
- ii) Derived from the reopening of the issuance on March 2005 for U.S. \$75 million and as a complement of the hedge strategy mentioned above, on June 6, 2005, the Company entered into a new derivative a Ps-USD CCS. The purpose of this agreement was to hedge the remaining portion of its U.S. dollar foreign exchange exposure resulting from the first issuance, and the totality of its U.S. \$75 million issuance. Under this agreement, Axtel will receive semiannual payments calculated based on the aggregate notional amount of U.S. \$136.25 million at an annual rate of 11%, and the Company will make semiannual payments calculated based on the aggregate of Ps. 1,480.4 (nominal value) at annual rate of 12.26%. This derivative instrument expired on December 15, 2008.
- iii) In August, 2007, the Company issued senior unsecured notes for U.S. \$275 million on a fixed rate. The Company decided to enter into a new derivative to cover the risk of exchange rate derived from this issuance denominated (“Currency Swap”). Under this agreement, Axtel will receive semiannual payments calculated based on the aggregate notional amount of U.S. \$275 million at a fixed annual rate of 7.625%, and the Company will make semiannual payments calculated based on the aggregate of Ps. 3,038.75 (nominal value) at a fixed annual rate of 8.54%.

As of December 31, 2009, the CCS information is as follows:

(Amounts in charts are expressed in millions)

Counterpart	Notional	Basic Conditions	Estimated fair value (USD)	
			2009	2008
Credit Suisse	Ps. 3,039 MXP \$275 USD	The Company pays fixed annual rate of 8.54% and receives fixed annual rate of 7.625%	\$4.3	\$12.4

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- iv) In September, 2009, the Company issued senior unsecured notes for U.S. \$ 300 million on a fixed rate. The Company decided to cover the risk of exchange rate derived from this issuance with some derivative financial instruments denominated “Currency Swap”. Under these agreements, Axtel will receive and will make payments detailed in the following table:

(Amounts in charts are expressed in millions)

Counterpart	Notional	Conditions	Estimated Fair Value
			(USD) 2009
Credit Suisse	Ps. 1,623 MXP \$125 USD	The Company pays fixed rate in pesos of 7.696% and receives fixed rate in usd of 9.00%	\$11.9
Deutsche Bank	Ps. 1,320 MXP \$100 USD	The Company pays fixed rate in pesos of 10.107% and receives fixed rate in usd of 9.00%	(\$1.4)
Merrill Lynch	Ps. 658 MXP \$50 USD	The Company pays fixed rate in pesos of 10.0825% and receives fixed rate in usd of 9.00%	(\$0.5)
Morgan Stanley	Ps. 327 MXP \$25 USD	The Company pays fixed rate in pesos of 10.080% and receives fixed rate in usd of 9.00%	(\$0.2)

For the year ended December 31, 2009, the change in the fair value of these CCS is an unrealized gain amount of U.S. \$9.52 million. This gain was recognized within the other comprehensive income section of equity, net of deferred taxes.

***Derivatives registered as trading***

The Company does not enter into contracts for derivative financial instruments for any purpose other than hedging. The Company does not speculate using financial instruments. However, the Company redeemed 35% of the issuance of U.S. \$250 million derived from the issuances of debt of December, 2003 and March, 2005. Originated by the closing of Swaps described in sections a) and b) from the paragraph “Cash flow hedges”, the Company stayed with an “over-hedge” in these derivatives therefore it decided to cover this excess of hedge with an inverse operation having the volatility of this portion being registered in the CFR. This operation is a CCS (Currency Swap). In this transaction the Company receives 12.26% over a notional amount of Ps. 950.7 million and pays 11% over the notional amount of U.S. \$87.5 million. According to the financial reporting standards this Swap does not comply with the requirements to be registered as a risk hedge; however it is considered as an economic hedge by the Company. This derivative instrument expired on December 15, 2008.

***Embedded derivatives***

The Company has conducted an initiative to identify, analyze and segregate if applicable, those contractual terms and clauses that implicitly or explicitly embed derivatives characteristics within financial or non financial agreements. These instruments are commonly known as embedded derivatives and do follow the same accounting treatment as of those free-standing contractual derivatives. Based on the above, the Company identified and recognized an amount of U.S. \$0.1 million from embedded derivatives effects during 2009 in the accounting records.

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**(b) Other financial instruments.**

During the months of July, August and September of 2009, the Company acquired call options denominated “Zero Strike Call” that have a notional of 26,096,700 CPOs of Axtel. The underlying of these instruments is the market value of the CPOs before indicated. The premium paid was equivalent to the market value of the notional plus fees. The strike price established was 0.000001 pesos per option. This instrument is redeemable in cash and not in kind. These are American options. At the Company’s decision, they can be exercised at any time, for a six months period and are extendable. The position is detailed in the following table:

<u>Counterparty</u>	<u>Notional</u>	<u>Conditions</u>	<u>Fair value (Millions of pesos) 2009</u>
Bank of America Merrill Lynch	26,096,700 CPOs	The Company receives in cash the market value of the notional	Ps. 309.5

At the year ended December 31, 2009 the change in the fair value of the Zero Strike Call resulted in an unrealized gain of Ps. 86,911 recognized in the CFR.

**(8) Related parties transactions and balances**

The transactions with related parties during the years ended December 31, 2009, 2008 and 2007, are mainly with Banamex, and are as follows:

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Telecommunication services revenue . . . . .	Ps.561,145	606,965	595,055
Commissions and administrative services . . . . .	11,406	11,960	19,490
Interest expense . . . . .	29,176	39,983	61,070
Rent expense . . . . .	15,145	25,757	24,198
Deferred revenue . . . . .	423,843	439,077	429,021
Installations services expense . . . . .	26,122	9,984	7,429
Others . . . . .	40,280	36,784	12,510
	<u>          </u>	<u>          </u>	<u>          </u>

The balances with related parties as of December 31, 2009 and 2008, included in accounts payable are as follows:

	<u>2009</u>	<u>2008</u>
Due to:		
GEN Industrial, S.A. de C.V. . . . .	Ps.132	84
Instalaciones y Desconexiones Especializadas, S.A. de C.V. . . . .	—	3,191
Neoris de Mexico, S.A. de C.V. . . . .	—	14,191
Total . . . . .	<u>Ps.132</u>	<u>17,466</u>

Compensation paid to key directors for the years ended December 31, 2009, 2008 and 2007 amounted to approximately Ps. 64 million, Ps. 51 million and Ps. 48 million, respectively. At December 31, 2009 the Company has debt as described in note 15.

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**(9) Inventories**

Inventories consist of the following:

	<u>2009</u>	<u>2008</u>
Telephones and call identification devices .....	Ps. 19,849	12,383
Installation material .....	32,731	32,069
Tools .....	19,745	13,854
Network spare parts .....	27,156	30,476
Others .....	71,200	50,116
Total inventories .....	<u>Ps.170,681</u>	<u>138,898</u>

**(10) Property, systems and equipment**

Property, systems and equipment are as follows:

	<u>2009</u>	<u>2008</u>	<u>Useful lives</u>
Land. ....	Ps. 167,331	167,331	
Building .....	263,659	263,659	25 years
Computer and electronic equipment .....	2,482,616	2,192,657	3 years
Transportation equipment .....	200,373	143,013	4 years
Furniture and fixtures.....	183,577	169,238	10 years
Network equipment .....	23,408,327	20,692,528	6 to 28 years
Leasehold improvements.....	372,363	343,270	5 to 14 years
Construction in progress .....	1,981,971	2,418,684	
Advances to suppliers .....	14,128	61,803	
	<u>29,074,345</u>	<u>26,452,183</u>	
Less accumulated depreciation.....	<u>13,863,726</u>	<u>11,145,735</u>	
Property, systems and equipment, net.....	<u>Ps.15,210,619</u>	<u>15,306,448</u>	

The Company has capitalized CFR as a complement of the acquisition cost, of Ps. 23,830 and Ps. 150,061 for the years ended December 31, 2009 and 2008, respectively.

As of December 31, 2009, certain financial leases amounting to approximately Ps. 12 million were guaranteed with the equipment acquired with those leases.

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**(11) Pre-operating expenses**

The capitalized pre-operating expenses incurred up to June 1999 and expenses incurred during 2000, 2004, 2005 and 2006 in opening new operations are as follows:

	<u>2009</u>	<u>2008</u>
Operating expenses .....	Ps.32,330	96,649
Salaries .....	24,933	231,963
Legal and financial advisory .....	—	118,238
Depreciation .....	—	10,275
Comprehensive financing result .....	—	(25,929)
Service and other revenues .....	—	(14,657)
Other .....	3,341	40,880
	<u>60,604</u>	<u>457,419</u>
Less accumulated amortization .....	<u>26,297</u>	<u>393,299</u>
Pre-operating expenses, net .....	<u>Ps.34,307</u>	<u>64,120</u>

As a consequence of the adoption of FRS C-8 in 2009 the Company canceled the unamortized balance at December 31, 2008 of the pre-operating expenses capitalized costs until December 31, 2002 for an amount of Ps. 19,436, net of deferred income tax for an amount of Ps. 7,558, against deficit, without a restatement of the financial statements of previous years.

**(12) Investment in shares of associated company and other permanent investments**

As of December 31, 2009, the investment in shares of associated company through Avantel is represented by a non-controlling 50% interest in the equity shares of Conectividad Inalámbrica 7GHZ, S. de R.L. The operation of this company consists in providing radio communication services in Mexico under the concession granted by the SCT. Such concession places certain performance conditions and commitments to this company, such as (i) filing annual reports with the SCT, including identifying main stockholders of the Company, (ii) reporting any increase in common stock, (iii) providing continuous services with certain technical specifications, (iv) to present a code of marketing strategies, (v) to register rates of service, (vi) to provide a bond and (vii) fulfilling the program of investments presented when the Company requested the concession.

Since the Company does not have effective control, this investment is accounted for by the equity method.



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Condensed financial information of the associated company as of December 31, 2009 and 2008 and for each of the years in the three-year period ended December 31, 2009, is as follows:

<b>Balance Sheet:</b>	<b>2009</b>	<b>2008</b>	
Current assets .....	Ps. 7,952	20,436	
Intangible assets .....	12,901	15,868	
Total assets.....	20,853	36,304	
Total liabilities .....	1,250	287	
Stockholders' equity .....	Ps. 19,603	36,017	
50% equity interest.....	Ps. 9,802	18,008	
<b>Statement of operations:</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>
Revenues from rent of frequency bands .....	Ps. —	7,510	5,602
Costs of services and operating expenses .....	(1,108)	(2,010)	(2,088)
Operating (loss) income .....	(1,108)	5,500	3,514
Other expenses .....	(14,940)	(7)	—
Comprehensive financial results .....	14	26	(368)
Deferred income tax .....	1,168	—	(287)
Net (loss) income.....	Ps.(14,866)	5,519	2,859
Equity in income of associated company .....	Ps. (7,433)	2,759	1,430

As of December 31, 2008, the liabilities of the Company with Conectividad Inalámbrica were Ps. 13,053.

**Other permanent investments**

The other permanent investments are as follows:

<b>December 31, 2009</b>	<b>Acquisition cost</b>
Eden Rock Communications .....	Ps.6,493

**(13) Intangible assets**

Intangible assets with defined useful lives consist of the following:

	<b>2009</b>	<b>2008</b>
Telephone concession rights Axtel .....	Ps.1,073,135	1,073,135
Telephone concession rights Avantel .....	114,336	114,336
Customers relationships .....	324,183	324,183
Trade name "Avantel" .....	186,074	186,074
	1,697,728	1,697,728
Less accumulated amortization.....	1,114,946	877,409
Intangible assets, net .....	Ps. 582,782	820,319

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***Concessions rights of the Company***

The Company has either obtained concessions as described below to offer telecommunications services or auctioned the following licenses over the spectrum of frequencies necessary to provide the services:

On June, 1996 Axtel obtained a concession to offer local and long distance telephony services, for a period of thirty years. To maintain this concession the Company needs to comply with certain conditions. It can be renewed for another period of thirty years;

- On September 15, 1995 Avantel obtained a concession to offer local and long distance telephony services, for a period of thirty years. To maintain this concession the Company needs to comply with certain conditions. It can be renewed for another period of thirty years;
- Two concessions in 929 MHz to offer mobile paging services;
- 50MHz in the 3.4GHz band. The licenses obtained allow nationwide coverage. The investment was Ps. 831,043 for a period of twenty years with an extension option;
- 56 MHz in the 7 GHz band, countrywide coverage, for a point-to-point transport (through the property of 50% of Conectividad Inalámbrica 7GHz, S. de R.L.);
- 60MHz for Point-to-Multi-Point in the 10.5GHz band nationwide. The acquisition of these twenty-year concessions, with an extension option, represented an investment of Ps. 160,931 for the Company;
- 120 MHz in three regions in 10.5 GHz band, for point-to-multi-point access (Concession originally granted to Avantel);
- 112MHz for Point-to-Point in the 15GHz band and a 100MHz in the 23GHz band, both with nationwide coverage. The acquisition of these twenty-year concessions, with an extension option, represented an investment of Ps. 81,161 for the Company;
- 56 MHz in the 15 GHz band, nationwide coverage, for point-to-point access and transport (Concession originally granted to Avantel);
- 268 MHz in the 23 GHz band, nationwide coverage, for point-to-point access and transport (Concession originally granted to Avantel);
- 112 MHz in the 37 to 38.6 GHz band, in 5 regions, for point-to-point transport (Concession originally granted to Avantel).

Each license of spectrum has a period of life of 20 years and it can be renovated for additional periods of 20 years as long as Axtel complies with all of its obligations, with all conditions imposed by the law and with any other condition that SCT imposes.

The concessions allow the Company to offer the following services:

- Local telephony service;
- National long distance telephony service;
- Selling or leasing of network capacity for the generation, transmission or reception of data, signs, images, voice, sounds and other type of information of any kind;
- Selling or leasing network capacity from other countries, including the leasing of digital circuits;

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- Value added services
- Operator services
- Mobile paging services
- Data services, video, audio conferences and videoconferences, except to restricted TV, continuous services of music or digital audio services; and
- Prepaid phone cards or credit phone cards

On November 2006, SCT granted the Company, as part of the concession of Axtel, a new permission to provide SMS (short messaging system) to its customers.

On September 15, 2009, SCT granted the Company a concession to install, operate and exploit a public telecommunications network to provide satellite television and audio services.

***Intangible assets arising from the acquisition of Avantel***

Derived from the acquisition of Avantel, the Company recorded certain intangible assets such as: trade name “Avantel”, customer relationships and telephone concession rights, whose value were determined by using an independent external expert appraiser at the acquisition date and accounted for in accordance to FRS B-7. The trade name and customer relationships are amortized in over a three-year period; meanwhile the concession is amortized over the remaining term of the concession on a straight-line basis. As of December 31, 2009 the values of the trade name “Avantel” and of customer relationships were totally amortized.

**(14) Other assets**

Other assets consist of the following:

	<u>2009</u>	<u>2008</u>
Notes issuance costs . . . . .	Ps.131,348	143,730
Long-term prepaid expenses . . . . .	85,054	92,003
Telmex / Telnor infrastructure costs . . . . .	68,279	68,279
Guarantee deposits . . . . .	43,730	38,003
Deferred financing costs . . . . .	41,016	41,016
World Trade Center concession rights . . . . .	22,474	22,474
Others . . . . .	<u>107,520</u>	<u>110,087</u>
	499,421	515,592
Less accumulated amortization . . . . .	<u>149,567</u>	<u>175,818</u>
Other assets, net. . . . .	<u><u>Ps.349,854</u></u>	<u><u>339,774</u></u>

***Notes issuance costs***

Notes issuance costs mainly consists of legal and audit fees, documentation, advising, printing, rating agencies, registration fees and out of pocket expenses incurred in relation to the issuance of notes payable and are amortized on a straight line basis over the life of the related debt. During 2009, derived from the prepayment of debt mentioned in note 15, the Company cancelled approximately Ps. 99,536 of note issuance costs related to those obligations less their accumulated amortization of Ps. 71,408.

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***Telmex / Telnor infrastructure costs***

As part of the opening of the telecommunications market in Mexico, new telecommunications companies must have interconnection with Telefonos de Mexico (Telmex) and Telefonos del Noroeste (Telnor). These two companies made agreements with the new entrants by which they must compensate Telmex and Telnor for their investments in infrastructure that Telmex / Telnor made in order to provide interconnection for the new telephone companies in Mexico. These costs are amortized over a period of fifteen years.

***Deferred financing costs related with the acquisition of Avantel***

The deferred financing costs incurred in the acquisition of Avantel will be amortized based upon the terms of the loans that they are related.

**(15) Long-term debt**

Long-term debt as of December 31, 2009 and 2008 consist of the following:

	2009	2008
U.S. \$275,000,000 in aggregate principal amount of 7 <sup>5</sup> / <sub>8</sub> % Senior Unsecured Notes due 2017. Interest is payable semiannually in February 1 and August 1 of each year. ....	Ps.3,591,143	3,723,033
U.S. \$300,000,000 in aggregate principal amount of 9% Senior Unsecured Notes due 2019. Interest is payable semiannually in arrears starting on March 22, 2010. ....	3,917,610	—
U.S. \$162,500,000 in aggregate principal amount of 11% Senior Unsecured Notes due 2013. Interest is payable semiannually in arrears on June 15, and December 15 of each year. Prepaid during the months of September and December 2009.....	—	2,199,973
Premium on Senior Notes issuance originated on the Senior Unsecured Notes with an aggregate principal of 162,500,000 with an interest rate of 11%, due 2013, was prepaid during the months of September and December 2009.....	—	22,743
Unsecured Syndicated Loan with Citibank, N.A., as the administrative agent, and Banamex as the peso agent, with a peso tranche in the aggregate amount of Ps. 1,042.4 and a U.S. dollar tranche in the aggregate amount of U.S. \$110.2. The final maturity date is February 2012, with quarterly principal repayments starting February 2010, with an interest rate for the tranche in pesos of THIE + 150 basis points, and the tranche in U.S. dollar of LIBOR + 150 basis points. ....	1,371,770	2,534,623
Change in the fair value of syndicated loan (See note 7(a)).....	39,740	250,083
Capacity lease agreement with Teléfonos de Mexico, S.A.B. de C.V. of approximately Ps. 800,000 payable monthly and expiring in 2011.....	280,336	415,184
Other long-term financing with several credit institutions with interest rates fluctuating between 3.60% and 7.20% for those denominated in dollars and THIE (Mexican average interbank rate) plus 1.5 and 3 percentage points for those denominated in pesos. ....	691,604	508,931
Total long-term debt .....	9,892,203	9,654,570
Less current maturities.....	944,553	296,106
Long-term debt, excluding current maturities .....	Ps.8,947,650	9,358,464

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Annual installments of long-term debt are as follows:

<u>Year</u>	<u>Amount</u>
2011.....	Ps. 896,309
2012.....	433,909
2013.....	68,940
2017 and thereafter.....	7,548,492
	<u>Ps.8,947,650</u>

Most significant changes in the long-term debt during 2009 and 2008 are as follows:

On September 22, 2009, the Company issued U.S. \$300 million of 10-year 9% unsecured senior notes. The notes mature on September 22, 2019. Interest will be payable semiannually and the senior notes bear interest at 9.0% commencing on March 22, 2010. The proceeds of this issuance were used to prepay the debt described as follows:

- (1) During the months of September, October and December of 2009, the Company redeemed U.S. \$162.5 million aggregate principal amount of its 11% Senior Unsecured Notes due 2013 equal to 100% of the remaining balance. The redemption was realized as follows:

Amounts in millions of USD:

<u>Date</u>	<u>Amount</u>	<u>Price</u>
September 22, 2009.....	\$128.5	105.750%
October 1, 2009.....	2.2	102.750%
December 15, 2009.....	31.8	103.667%
	<u>\$162.5</u>	

- (2) Additionally, the Company paid all accrued interest at the date of redemption. The premium paid in these transactions was U.S. \$8.6 million, which was included in the comprehensive financial results (“CFR”).
- (3) On September 25, 2009, the Company prepaid U.S. \$85.0 million of the portions in USD of the Syndicated Loan, including accrued interest at the date of redemption.

On February 2, 2007, the Company issued U.S. \$275 million of 10-year unsecured senior notes. This issuance matures on February 1, 2017. Interest will be payable semiannually and the senior notes bear interest at 75/8% beginning on August 1, 2007. The proceeds of this issuance were used to prepay the bridge financing related to the December 2006 acquisition of Avantel. All the subsidiaries of Axtel are guarantors for this issuance.

Some of the debt agreements that remain outstanding establish certain covenants, the most significant of which refer to limitations on dividend payments and comprehensive insurance on pledged assets. For the year ended December 31, 2009, the Company was in compliance with all of its covenants.

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**(16) Other accounts payable**

As of December 31, 2009 and 2008 other accounts payable consist of the following:

	<u>2009</u>	<u>2008</u>
Guarantee deposits (note 21c).....	Ps.169,763	175,998
Interest payable (note 21c) .....	108,925	103,709
Guarantee deposit (SR Telecom) .....	10,300	10,678
Other .....	82,515	67,629
	<u>Ps.371,503</u>	<u>358,014</u>

**(17) Employee benefits**

The cost, obligations and other elements of pensions, seniority premiums and severance compensations plans for reasons other than restructuring have been determined based on computations prepared by independent actuaries at December 31, 2009 and 2008. The components of the net periodic cost for the years ended December 31, 2009, 2008 and 2007 are as follows:

	<u>2009</u>		
	<u>Termination</u>	<u>Retirement</u>	<u>Total</u>
Net periodic cost:			
Service cost.....	Ps. 9,917	626	10,543
Interest cost.....	4,946	288	5,234
Amortization of transition obligations.....	2,300	—	2,300
Amortization of prior service cost and plan modifications .....	(3,596)	(27)	(3,623)
Net periodic cost .....	<u>Ps.13,567</u>	<u>887</u>	<u>14,454</u>
	<u>2008</u>		
	<u>Termination</u>	<u>Retirement</u>	<u>Total</u>
Net periodic cost:			
Service cost.....	Ps. 9,231	500	9,731
Interest cost.....	3,884	192	4,076
Amortization of transition obligation.....	2,301	—	2,301
Variances in assumptions and experience adjustments.....	(2)	23	21
Amortization of prior service cost and plan modifications .....	(3,596)	(27)	(3,623)
Prior service cost (2007 unamortized items) .....	4,136	—	4,136
Net periodic cost .....	<u>Ps.15,954</u>	<u>688</u>	<u>16,642</u>

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	<b>2007</b>		
	<b>Seniority Premium</b>	<b>Severance payments</b>	<b>Total</b>
Net periodic cost:			
Service cost .....	Ps.1,677	6,019	7,696
Interest cost .....	281	1,296	1,577
Amortization of transition obligation .....	1	3,453	3,454
Variances in assumptions and experience adjustments .....	(53)	(1,782)	(1,835)
Inflationary effect .....	72	360	432
Net periodic cost .....	<u>Ps.1,978</u>	<u>9,346</u>	<u>11,324</u>

The actuarial present value of benefit obligations of the plans at December 31, 2009 is as follows:

	<b>2009</b>		
	<b>Termination</b>	<b>Retirement</b>	<b>Total</b>
Accumulated benefit obligation (ABO) .....	<u>Ps.51,021</u>	<u>8</u>	<u>51,029</u>
Projected benefit obligation (PBO) .....	Ps.63,055	3,388	66,443
Unrecognized items:			
Transition asset .....	(6,903)	—	(6,903)
Variances in assumptions .....	10,788	494	11,282
Actuarial loss .....	—	(192)	(192)
Net projected liability .....	<u>Ps.66,940</u>	<u>3,690</u>	<u>70,630</u>

The actuarial present value of benefit obligations of the plans at December 31, 2008 is as follows:

	<b>2008</b>		
	<b>Termination</b>	<b>Retirement</b>	<b>Total</b>
Accumulated benefit obligation (ABO) .....	<u>Ps.55,238</u>	<u>—</u>	<u>55,238</u>
Projected benefit obligation (PBO) .....	Ps.55,238	2,759	57,997
Unrecognized items:			
Transition asset .....	(9,204)	—	(9,204)
Variances in assumptions .....	14,385	521	14,906
Actuarial loss .....	—	(354)	(354)
Net projected liability .....	<u>Ps.60,419</u>	<u>2,926</u>	<u>63,345</u>



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The most significant assumptions used in the determination of the net periodic cost of plan are the following:

	<u>2009</u>	<u>2008</u>
Discount rate (net of inflation) used to reflect the present value of obligations . . . . .	8.50%	8.00%
Rate of increase in future salary levels . . . . .	5.50%	5.00%
Amortization period of unrecongized items . . . . .	5 years	5 years
Average remaining labor life of employees . . . . .	20.5 years	20.6 years

**(18) Income (IT) and asset taxes (AT), Flat Tax (IETU) and employee statutory profit sharing (ESPS).**

According to the actual tax laws, companies will be required to pay the greater of their IETU or IT. If IETU is payable, the payment will be considered final and not subject to recovery in subsequent years. The actual IT tax law on December 31, 2009, establish a rate applicable of 28% and, according to the actual tax laws and beginning January 1, 2010, the IT rate is 30% from 2010 to 2012, 29% for 2013 and 28% for 2014 and thereafter. The IETU rate is 17% for 2009 and 17.5% for 2010 and thereafter.

According to financial accounting standards, management performed an evaluation of the tax that the Company and its subsidiaries will be subject for the years ended December 31, 2009 and 2008. The Company determined that certain subsidiaries will be subject to IETU. As a result, the Company canceled IT recorded for an amount of Ps. 214,003 and registered deferred IETU for an amount of Ps. 32,046 as of December 31, 2008. For presentation purposes of deferred taxes, deferred IETU and IT are presented jointly.

The income tax expense attributable to income (loss) before income taxes differed from the amounts computed by applying the Mexican statutory rates of 28% for IT to income (loss), as a result of the items mentioned below:

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Computed “expected” tax (expense) benefit . . . . .	Ps.(102,271)	281,304	(244,374)
Increase (decrease) resulting from:			
Effects of inflation, net . . . . .	124,088	210,221	(1,432)
Change in valuation allowance . . . . .	(119,882)	86,450	(101,463)
Accelerated depreciation . . . . .	—	(76,829)	(43,550)
Non—deductible expenses . . . . .	9,958	(22,903)	(5,757)
Deferred IETU . . . . .	11,127	32,046	—
Deferred employee’s profit sharing . . . . .	—	—	13,594
Cancellation of the deferred IT . . . . .	—	(214,003)	—
Expired operating loss carryforwards . . . . .	(154,250)	—	—
Adjustments to deferred tax assets and liabilities for enacted changes in tax rates . . . . .	44,114	—	—
Other . . . . .	5,695	5,287	(218)
IT and IETU (expense) benefit . . . . .	Ps.(181,421)	301,573	(383,200)

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The tax effects of temporary differences that gave rise to significant portions of the deferred tax assets and deferred tax liabilities as of December 31, 2009 and 2008 are presented below:

	<u>2009</u>	<u>2008</u>
Deferred tax assets:		
Net operating loss carryforwards .....	Ps. 726,134	1,071,970
Allowance for doubtful accounts .....	432,925	363,091
Accrued liabilities and others .....	136,986	169,693
Recoverable AT .....	382,104	423,003
Deferred IETU .....	61,098	32,046
Premium on bond issuance .....	—	2,656
Property, systems and equipment .....	422,543	55,459
Total gross deferred tax assets .....	<u>2,161,790</u>	<u>2,117,918</u>
Less valuation allowance .....	<u>726,245</u>	<u>606,363</u>
Net deferred tax assets for IT and Deferred IETU .....	<u>1,435,545</u>	<u>1,511,555</u>
Deferred tax liabilities:		
Telephone concession rights .....	149,889	211,331
Fair value of derivative instruments .....	58,067	45,339
Intangible and other assets .....	77,082	62,562
Total deferred tax liabilities .....	<u>285,038</u>	<u>319,232</u>
Deferred tax assets, net for IT and Deferred IETU .....	<u>Ps.1,150,507</u>	<u>1,192,323</u>

The rollforward for the net deferred tax asset for the years ended December 31, 2009 and 2008 is presented below:

	<u>2009</u>	<u>2008</u>
Balances at beginning of year .....	Ps.1,192,323	936,089
Deferred IT (expense) benefit .....	(119,431)	286,045
Deferred IETU benefit .....	29,052	32,046
Deferred IT from the application effect of FRS C—8 .....	7,558	—
Deferred IT of derivative financial instruments .....	41,005	(61,857)
Balances at end of year .....	<u>Ps.1,150,507</u>	<u>1,192,323</u>

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon of future taxable income during periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences, net of the existing valuation allowances at December 31, 2009. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced.

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According to the IT law, the tax loss of a year, restated by inflation, may be carried to the succeeding ten years. The tax losses have no effect on ESPS. As of December 31, 2009, the tax loss carryforwards and AT pending of recovery expire as follows:

<u>Year</u>	<u>Inflation-adjusted tax loss carryforwards</u>	<u>Tax on assets</u>
2010 .....	Ps. 403,238	—
2011 .....	156,547	75,478
2012 .....	424,919	52,962
2013 .....	497,554	83,367
2014 .....	98,989	80,010
2015 .....	—	34,370
2016 .....	21,648	29,776
2017 .....	—	77,855
2018 .....	965,902	—
	<u>Ps.2,568,797</u>	<u>433,818</u>

Tax loss carry forwards and AT pending of recovery includes Ps. 125,166 and Ps. 51,714, respectively from companies in which deferred IETU was calculated.

The tax effects of temporary differences that gave rise to deferred employee's profit sharing as of December 31, 2009 and 2008 are presented below:

	<u>2009</u>	<u>2008</u>
Deferred ESPS assets:		
Accrued liabilities .....	Ps. 2,016	1,606
Accrued for labor obligations .....	7,063	6,334
Other payroll accruals .....	4,352	3,808
Net deferred ESPS asset .....	<u>13,431</u>	<u>11,748</u>
Deferred ESPS liabilities:		
Deferred income .....	2,079	1,243
Property, systems and equipment .....	907	2,481
Other .....	738	209
Total deferred ESPS liability .....	<u>3,724</u>	<u>3,933</u>
Deferred ESPS asset, net .....	<u>Ps. 9,707</u>	<u>7,815</u>

The rollforward for the net deferred employee's profit sharing asset for the years ended December 31, 2009 and 2008 is presented below:

	<u>2009</u>	<u>2008</u>
Balances at beginning of year .....	Ps.7,815	14,180
Deferred ESPS benefit (expense) .....	1,892	(6,365)
Balances at end of year .....	<u>Ps.9,707</u>	<u>7,815</u>

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As of December 31, 2009, 2008 and 2007, employees' statutory profit sharing was Ps.11,152, Ps.7,974 and Ps. 6,088 respectively.

**(19) Stockholders' equity**

The principal characteristics of stockholders' equity are described below:

*(a) Capital stock structure*

At December 31, 2009, the Company has 8,769,353,223 shares issued and outstanding. Company's shares are divided in two Series: Series A and B; both Series have two type of classes, Class "I" and Class "II", with no par value. From the total shares, 96,636,627 shares are Series A and 8,672,716,596 shares are Series B. At December 31, 2009 the Company has only issued Class "I" shares. Also, at December 31, 2009 all shares issued are part of the fixed portion.

On August 31, 2007, the stockholders' approved a three-for-one stock split (the split). The split became effective on October 8, 2007. The proportional equity interest participation of existing stockholders' did not change as a result of the split. Following table shows the effects of the split:

	<u>Number of Shares before the Split</u>	<u>Number of Shares after the Split</u>
Series A Shares .....	32,212,209	96,636,627
Series B Shares .....	<u>2,890,905,532</u>	<u>8,672,716,596</u>
Total of Shares .....	<u>2,923,117,741</u>	<u>8,769,353,223</u>

The percentages of shares holding did not change as a result of the split. For comparison purposes, the number of shares is presented adjusted for the effects of the split.

The following represents a rollforward of Company's shares for the years ended December 31, 2009, 2008 and 2007, after considering the effects of the split:

	<u>Subscribed and paid shares</u>	<u>Common stock</u>	<u>Additional paid-in capital</u>
Balances as of December 31, 2006 .....	8,522,810,598	Ps. 8,677,782	547,131
Subscribed and paid shares .....	<u>246,542,625</u>	<u>192,280</u>	<u>194,540</u>
Balances as of December 31, 2007 .....	8,769,353,223	Ps. 8,870,062	741,671
Absorption of accumulated deficit from prior years in 2008 .....	<u>—</u>	<u>(1,307,987)</u>	<u>—</u>
Balances as of December 31, 2008 and 2009 .....	<u>8,769,353,223</u>	<u>Ps. 7,562,075</u>	<u>741,671</u>

As of December 31, 2009 and 2008, the common stock of the Company is Ps. 6,625,536 (nominal value), represented by 96,636,627 common shares, with no nominal value, Class "I", "A" Series, subscribed and paid, and 8,672,716,596 common shares, with no nominal value, Class "I", "B" Series, subscribed and paid.

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At an ordinary stockholders meeting held on April 23, 2008, the stockholders approved the reduction of the caption named “Restatement of capital stock” on Ps. 1,307,987 to reclassify the absorption of accumulated deficit of prior years.

During July 2008 the Company began an own shares repurchase program which was approved at an ordinary shareholders’ meeting held on April 23, 2008 for up to Ps. 440 million. As of December 31, 2008 the Company had repurchased 26,096,700 CPO’s (182,676,900 shares). During the months of July, August and September the CPOs purchased through the repurchase program were resold in the market.

The acquisition of Avantel also included a Series B Shares Subscription Agreement (“Subscription Agreement”) with Tel Holding, an indirect subsidiary of Citigroup, Inc., for an amount equivalent to up to 10% of Axtel’s common stock. To give effect to the above, the Company obtained stockholder approval (i) to increase its capital by issuing Series B Shares in a number that was sufficient for Tel Holding to subscribe and pay Series B Shares (in the form of CPOs) representing up to a 10% equity participation in Axtel; and (ii) for the subscription and payment of the Series B Shares that represented the shares subscribed by Tel Holding and any shares subscribed by stockholders that elected to subscribe and pay for additional Series B Shares in exercise of their preferential right granted by the Mexican General Corporation Law.

On December 22, 2006 pursuant to the Subscription Agreement, the Company received notice from Tel Holding confirming that it acquired 533,976,744 Series B Shares (represented by 76,282,392 CPOs) from the Mexican Stock Exchange (Bolsa Mexicana de Valores, or “BMV”) and confirming its intention to subscribe and pay for 246,453,963 new Series B Shares (represented by 35,207,709 CPOs). The new Series B Shares were subscribed and paid for, which we refer to herein as the “Equity Subscription,” by Tel Holding through the CPOs Trust on January 4, 2007.

***(b) Stockholders’ equity restrictions***

Stockholders’ contributions, restated for inflation as provided in the tax law, totaling Ps. 7,701,697 may be refunded to stockholders tax-free.

No dividends may be paid while the Company has a deficit. Some of the debt agreements mentioned in note 15 establish limitations on dividend payment.

***(c) Comprehensive income***

The comprehensive income reported on the statements of stockholders’ equity represents the results of the total performance of the Company during the year, and includes the items mentioned below which, in accordance with Mexican FRS, are reported directly in stockholders’ equity, except for net income.

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Net income (loss).....	Ps. 176,400	(700,324)	490,996
Fair value of derivative instruments.....	(147,342)	220,918	(16,378)
Deferred IT of derivative financial instruments.....	41,005	(61,857)	4,586
Comprehensive income (loss) .....	<u>Ps. 70,063</u>	<u>(541,263)</u>	<u>479,204</u>

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**(20) Telephone services and related revenues**

Revenues consist of the following:

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Local calling services .....	Ps. 4,649,467	5,242,577	5,336,628
Long distance services .....	1,188,669	1,286,127	1,532,176
Data services .....	2,451,951	2,500,473	2,513,751
International traffic .....	1,323,810	982,937	1,210,233
Other services .....	1,354,980	1,560,287	1,597,822
	<u>Ps.10,968,877</u>	<u>11,572,401</u>	<u>12,190,610</u>

**(21) Commitments and contingencies**

As of December 31, 2009, the Company has the following commitments and contingencies:

- (a) On September 1, 2008, the Ministry of Communications and Transport (*Secretaría de Comunicaciones y Transportes* “SCT”), issued four rulings resolving four administrative review proceedings regarding interconnection disagreements that were previously filed before the Federal Telecommunications Commission (*Comisión Federal de Telecomunicaciones* “COFETEL”) against the following companies: Radiomovil Dipsa, S.A. de C.V. (“Telcel”), Iusacell PCS, S.A. de C.V. and others (“Grupo Iusacell”), Pegaso PCS, S.A. de C.V. and others (“Grupo Telefonica”) and Operadora Unefon, S.A. de C.V. (“Unefon”).

The resolutions issued by the SCT, consider, firstly, the application of new rates regarding consumption beginning in September 2008, and secondly, the retroactive application of those rates. In the case of Telcel being effective since January 1, 2008, and for the case of the other mobile operators (Grupo Iusacell, Grupo Telefonica and Unefon), being effective since October 2006.

Therefore, effective as of September 2008, the mobile carriers are obligated to bill the Company for the termination of calls in mobile phones under the modality of “Calling Party Pays” according to the terms of the resolutions (using rates based on the real duration of the call), and in addition, according to such resolutions, the Company could claim the amounts that the Company has paid in excess during the periods referred to under the resolutions mentioned, that is, the difference between the interconnection rates applied by the mobile carriers and paid by the Company during such period, and the rates established by the SCT in the resolutions.

As of December 31, 2009, according to the resolutions of the SCT and using some preliminary information of the Company, both Axtel and Avantel would have paid in excess to Telcel approximately the amount of Ps. 397.7 million, and to the rest of the mobile operators, the amount of Ps. 396.6 million, as shown in the following table:

<u>Telcel</u>	<u>Axtel</u>	<u>Avantel</u>	<u>Total</u>	<u>Other Operators</u>	<u>Axtel</u>	<u>Avantel</u>	<u>Total</u>
2006 .....	—	—	—	2006 .....	Ps. 53.5	7.7	61.2
2007 .....	—	—	—	2007 .....	181.7	25.9	207.6
January – July 2008....	Ps.355.0	42.7	397.7	January – July 2008...	112.8	15.0	127.8
Total .....	<u>Ps.355.0</u>	<u>42.7</u>	<u>397.7</u>	Total .....	<u>Ps.348.0</u>	<u>48.6</u>	<u>396.6</u>

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As a result of the resolutions issued by the SCT, the Company acknowledged that since August 2008 and thereafter, the interconnection rate for termination authorized for 2008, was of Ps. 0.5465 per minute for Telcel and Ps. 0.6032 per minute for the rest of the carriers; and the authorized rates for 2009 were Ps. 0.5060 per real minute for Telcel, and Ps. 0.6032 per real minute for the rest of the carriers. Applying the concept of non-discriminatory treatment, Avantel also adopted the rates mentioned above. The rates that Axtel and Avantel were paying before the resolutions, amounted to Ps. 1.3216 for each real minute for Telcel and Ps. 1.21 for each rounded minute for the rest of the mobile carriers. Nevertheless, the mobile carriers remain invoicing the Company for the termination of traffic under the modality of “Calling Party Pays” applying the rates previous to the resolutions mentioned above. As of December 31, 2009, the difference between the amounts paid by the Company according to the new rates established by the SCT, and the amounts invoiced by the mobile carriers, amounted to approximately Ps. 950 million not including Value Added Tax.

The Company is aware that Telcel and the other mobile carriers have filed before the Federal Courts, their non-conformity with respect to the resolutions issued by the SCT mentioned, and there is a contingency for the Company (Axtel and Avantel) in case that the Courts rule against these resolutions, and that as a result, different rates are established in comparison to those established by the SCT. The contingency would be the difference between the rates established by SCT, and those rates established by the Courts under the respective resolutions, such contingency in case that these rates are higher than Ps. 0.5465 for each real minute for Telcel and Ps. 0.6032 for each real minute for the rest of the mobile carriers. The Company’s management believes that the Company has the necessary elements to prevail under these proceedings before the Court, therefore, since August 2008 and thereafter, it has recognized the cost based on Ps. 0.5465 per each real minute for Telcel and Ps. 0.6032 per each minute for the rest of the mobile carriers.

With respect to the possibility of the Company to recover the payments made in excess of applicable amounts due under the resolutions for periods prior to August 2008, it is important to mention that collection or recovery of such amounts is not automatic, therefore, in order to collect or recover, among other alternatives, the Company may initiate ordinary mercantile trials against the mobile carriers. In this case any claimed amounts by the Company in such litigation will be subject to the interpretation of the Judges based upon the evidence and documents presented by the parties, that in case that the Company decides to follow this alternative. The above mentioned, considering the characteristics and complexity of the resolutions of the SCT and their effects, plus the fact that there is little or no precedents, it is very likely that these proceedings will be lengthy. As of December 31, 2009, the Company has not recognized the benefit of any such possible recovery.

After evaluating the actual status of the foregoing proceedings and according to the available information and information provided by the legal advisors, the management of the Company considers that there are enough elements to maintain the actual accounting treatment, and that at the end of the legal process the interests of the Company will prevail.

The management of the Company aware of the fact Telcel and the other mobile operators have asked the federal courts for the suspension of the resolutions by the SCT, but those suspensions are still not binding or compulsory for the Company, except for the case of Grupo Telefonica, which suspension was served to the Company, nevertheless, it ceased to be in effect due to the fact that the Company decided to present a bail. Due to the above, the actual interconnection rates applicable to the Company are the ones established in the SCT’s resolution dated September 1 2008.



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- (b) In March 2009, the COFETEL resolved an interconnection disagreement proceeding existing between the Company (Axtel) and Teléfonos de México, S.A.B. de C.V. (“Telmex”) related to the rates for the termination of long distance calls from the Company to Telmex with respect to year 2009. In such administrative resolution, the COFETEL approved a reduction in the rates for termination of long distance calls applicable to those cities where Telmex does not have interconnection access points. These rates were reduced from Ps. 0.75 per minute to U.S. \$0.0105 or U.S. \$0.0080 per minute depending on the place where the Company delivers the long distance call.

Nevertheless, Telmex remains invoicing the Company for the termination of long distance calls applying the rates that were applicable prior to the resolutions mentioned above. As of December 31, 2009, the difference between the amounts paid by the Company to Telmex according to the new rates, and the amounts invoiced by Telmex, amount to approximately to Ps. 764 million, not including VAT.

Telmex filed for a nullification proceeding before the Federal Tax and Administrative Court (*Tribunal Federal de Justicia Fiscal y Administrativa*) requesting the nullification of COFETEL’s administrative resolution. The Company (Axtel and Avantel) have a contingency in case that the Federal Tax and Administrative Court rules against the Company, and that as a result, establishes different rates compared to those established by COFETEL. Telmex obtained a suspension for the application of the interconnection rates established by COFETEL, such suspension was effective beginning on January 26, 2010, but ceased to be in force and effect as of February 11, 2010, since the Company decided to exercise its right to leave without effect the suspension by guaranteeing any damages that could be caused to Telmex.

On February 2010, the COFETEL resolved an interconnection disagreement proceeding existing between the Company (Avantel) and Telmex related to the rates for the termination of long distance calls from the Company to Telmex with respect to year 2009. In such administrative resolution, the COFETEL approved a reduction in the rates for termination of long distance calls applicable to those cities where Telmex does not have interconnection access points. These rates were reduced from Ps. 0.75 per minute to U.S. \$0.0126, U.S. \$0.0105 or U.S. \$0.0080 per minute, depending on the place where the Company delivers the long distance call. Based on this resolution, the Company paid in excess approximately Ps. 20 million. The management of the Company considers that Telmex will likely challenge the resolution.

The Company believes that the rates under COFETEL’s resolution will prevail, therefore has recognized the cost based on the tariffs approved by COFETEL. Due to the fact that the proceedings followed by Telmex are recent, the Company and its legal advisors are evaluating the steps to be followed .

- (c) On January 24, 2001, an agreement was entered into with Global Towers Communications Mexico, S. de R.L. de C.V. (Formerly Spectrasite Communications Mexico, S. de R.L. de C.V.), which agreement contemplated an expiration date on January 24, 2004, whereby Global Towers was to provide to the Company with services for the location, construction, setting up and selling of sites within the Mexican territory. As part of the operation, the Company agreed to lease from Global Towers 650 sites in a time frame period of three years.

On January 24, 2001, the Company received 13 million dollars from Global Towers to secure the acquisition of the 650 sites at 20,000 dollars per site. According to the agreement, these funds are not subject to restrictions with respect to their use and destination. However, the agreement contemplates the payment of interest at a Prime Rate in favor of Global Towers on the warranty amount corresponding to the number of sites that as of June 24, 2004, were not sold or leased in accordance with the terms of the agreement.

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During 2002, Global Towers filed an Ordinary Mercantile Trial against the Company before the Thirtieth Civil Court of Mexico City, claiming the refund of the guarantee deposit mentioned above, plus interest and trial-related expenses; the Company counterclaimed Global Towers because the latter terminated the agreement unilaterally.

On April 1, 2008, the trial court ruled against us ordering Axtel to return the deposit and applicable interests. The Company appealed the trial court's order before the Superior Court of Appeal.

On August 4, 2008, the Superior Court of Appeal ruled in favor of the Company releasing and discharging it from any liability whatsoever under the contract signed with Global Towers and ordering the latter to pay the Company for any damages caused to the Company for the non-compliance by Global Towers to perform its obligations under said contract. Global Towers filed a Constitutional Trial (*Juicio de Amparo*) against the resolution of the Superior Court of Appeal.

On March 2009, the Superior Court of Justice ruled again in favor of the Company releasing and discharging the Company from any liability whatsoever under the contract with Global Towers and ordering Global Towers to pay the Company for any damages caused to the Company resulting from the non-compliance by Global Towers to perform its obligations under the contract. Global Towers filed a Constitutional Trial (*Juicio de Amparo*), and as of today the resolution is pending.

As of December 31, 2009, the Company recognized a liability to cover interests amounting to Ps. 108,925, plus the principal amount, recorded in the "other accounts payable" line item in the balance sheet.

- (d) During September and November 2005, Avantel Infraestructura filed before the Federal Court of Tax and Administrative Justice a lawsuit against the resolution of the "negativa ficta" (automatic negative ruling as a result of lack of answer), arising due to the fact that there was no resolution during the 3 months period as stated under the Federal Tax Code (*Código Fiscal de la Federación*) with respect to the request for a confirmation of criteria in the sense that Avantel Infraestructura is not obliged to pay duties under article 232 Section I of the Federal Duties Law, with respect to the use of exclusive economic geographic zone in Mexico related to certain landing points in "Playa Niño", region 86, Benito Juarez, Itanah Tulum, Carrillo Puerto, and Quintana Roo.

The suit was turned for study and resolution to the 5th Metropolitan Regional Court of the Federal Court of Tax and Administrative Justice, who declared the annulment of the "negative ficta", in order for the authority being sued to issue another resolution legally supported, considering the terms of the resolution.

Not in conformity with the ruling pronounced by the Federal Court of Tax and Administrative Justice, Avantel filed an *Amparo Directo* (Constitutional Review), while at the same time, the authority started a Tax Review, proceedings that are still pending to be sent to the Federal Collegiate Court for their study and resolution.

- (e) The Company is involved in a number of lawsuits and claims arising in the normal course of business. It is expected that the final outcome of these matters will not have significant adverse effects on the Company's financial position and results of operations.
- (f) In compliance with commitments made in the acquisition of concession rights, the Company has granted surety bonds to the Federal Treasury and to the Ministry of Communication and Transportation amounting to Ps. 4,603 and to other service providers amounting to Ps. 669,269.

**AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**

**Notes to the Consolidated Financial Statements—(Continued)**  
**December 31, 2009, 2008 and 2007**  
**(Thousands of Mexican pesos)**

- (g) The concessions granted by the Ministry of Communications and Transportation (SCT), mentioned in note 2, establish certain obligations to the Company, including, but not limited to: (i) filing annual reports with the SCT, including identifying main stockholders of the Company, (ii) reporting any increase in common stock, (iii) providing continuous services with certain technical specifications, (iv) filing monthly reports about disruptions, (v) filing the services' tariff, and (vi) providing a bond.
- (h) The Company leases some equipment and facilities under operating leases. Some of these leases have renewal clauses. Lease expense for 2009, 2008 and 2007 was Ps. 483,939, Ps. 414,343 and 457,457, respectively.

The annual payments under these leases as of December 31, 2009 are as follows:

	Contracts in:	
	Pesos (thousands)	Dollars (thousands)
2010 .....	Ps.170,121	\$ 7,144
2011 .....	127,368	3,670
2012 .....	101,552	2,195
2013 .....	86,002	2,084
2014 .....	76,184	2,043
2015 and thereafter .....	204,276	1,742
	Ps.765,503	\$18,878

- (i) As of December 31, 2009, the Company has placed purchase orders which are pending delivery from suppliers for approximately Ps. 950,637.
- (j) As of December 31, 2009, there was a letter of credit for U.S. \$34 million issued by Banamex in favor of Telmex for the purpose of guaranteeing the Company's acquired obligations in several interconnection agreements. The amounts under the letter of credit were drawn by Telmex in the month of January 2010, in respect of amounts already owed by Avantel to Telmex. The Company, supported by its legal advisors, is evaluating the steps to be followed.

In January 15, 2010 Banamex granted Axtel a U.S. \$32 million working capital loan at market conditions which matures on July 15, 2010.

**(22) Recently issued accounting standards**

The CINIF has issued the following FRS, applicable for years beginning on or after January 1, 2010 or 2011, as indicated.

- (a) **FRS B-5 "Segment information"**—FRS B-5 is effective as of January 1, 2011. Changes as compared to superseded Bulletin B-5 "Segment Information" include the following:
- Senior management regularly discloses information by operating segment and does not require the segmentation of information into primary and secondary or into segments identified based on products or services (economic segments), geographical areas or uniform customer groups. Additionally, it requires disclosure by entity as a whole, information on its products or services, geographical areas and principal customers and suppliers).
  - FRS B-5 does not require that the entity's business areas be subject to different risks to qualify as operating segments.

**AXTEL, S. A. B. DE C. V. AND SUBSIDIARIES**

**Notes to the Consolidated Financial Statements—(Continued)**  
**December 31, 2009, 2008 and 2007**  
**(Thousands of Mexican pesos)**

- FRS B-5 allows business areas in pre-operating stage to be catalogued as operating segments.
- FRS B-5 requires disclosure by segment and separately, revenue and interest expense as well as all other components of comprehensive financial results (CFR). In specific cases, the FRS B-5 permits disclosure of net interest income.
- FRS B-5 requires disclosure of the liability amounts included in the usual operating segment information normally used by senior management in making the entity's operating decisions.

Management estimates that the initial effects of this new FRS will not be material.

- (b) **FRS B-9 “Interim financial reporting”**—FRS B-9 is effective as of January 1, 2010. Changes as compared to superseded Bulletin B-9 “Interim financial reporting” include the following:
- FRS B-9 requires that the interim financial information includes a comparative and condensed balance sheet, income statement, statement of stockholders' equity and statement of cash flows and, for non-profit entities, it expressly requires the presentation of a statement of activities.
  - FRS B-9 establishes that the financial information at the end of an interim period should be presented comparatively with the equivalent interim period of the immediately preceding year and, in the case of the balance sheet, compared also to such financial statement at the immediately preceding year-end date.
  - FRS B-9 includes and defines new terminology.
- (c) **FRS C-1 “Cash and cash equivalents”**—FRS C-1 supersedes Bulletin C-1 “Cash” and is effective as of January 1, 2010. The principal changes with respect to the former standard include the following:
- FRS C-1 requires the presentation of cash and cash equivalents, restricted, within the balance sheet caption of “Cash and cash equivalents”.
  - The term “demand temporary investments” is replaced by “available demand investments”.
  - To be identified as cash equivalents, the investments should be highly liquid, for example those with original maturities of three months or less when purchased.
  - FRS C-1 includes the definition of the terms: acquisition cost, restricted cash and cash equivalents, highly liquid investments, net realizable value, nominal value and fair value.

Management estimates that the initial effects of this new FRS will not be material.

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