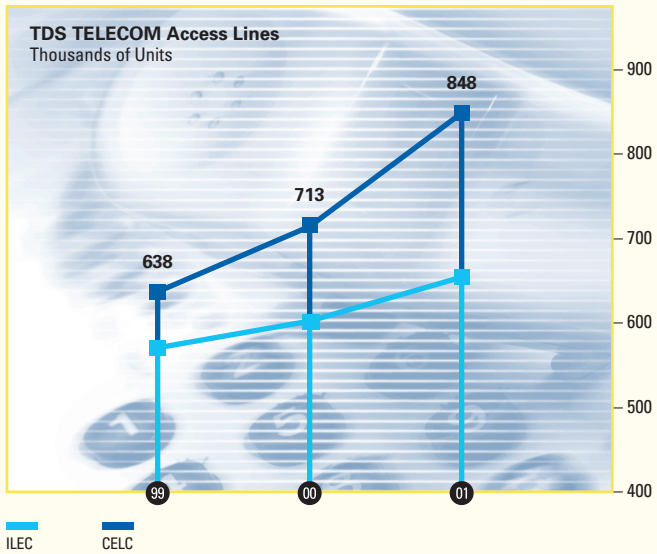


# Telephone and Data Systems, Inc.

## Management’s Discussion and Analysis of Results of Operation and Financial Condition

### Wireline Telephone Operations

TDS operates its wireline telephone business through TDS Telecommunications Corporation (“TDS Telecom”), a wholly-owned subsidiary. TDS Telecom served 847,900 access lines at the end of 2001, an increase of 134,600 lines over 2000. At the end of 2000, TDS Telecom served 713,300 lines, an increase of 75,700 lines over 1999. TDS Telecom provides service through local telephone operations, or Incumbent Local Exchange carrier (“ILEC”) companies, and through Competitive Local Exchange carrier (“CLEC”) companies.



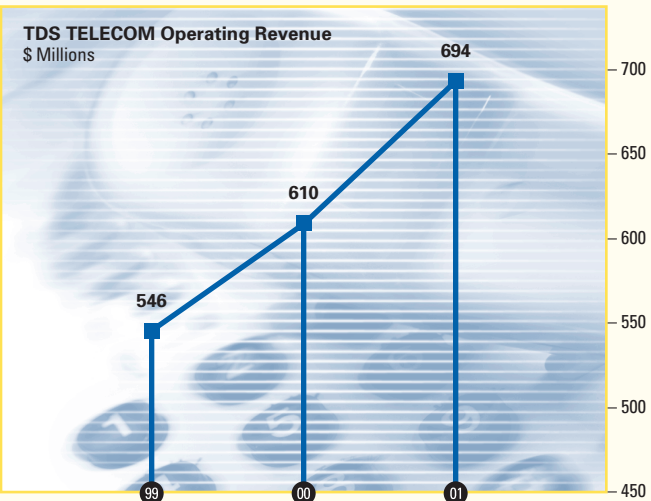
TDS Telecom’s local telephone companies served 650,700 access lines at the end of 2001 compared to 601,200 at the end of 2000 and 571,700 at the end of 1999. Local telephone operations have grown through acquisitions and internal growth. Acquisitions added 43,400 lines in 2001 and 10,200 lines in 2000, and internal growth added 6,100 lines in 2001 and 19,300 lines in 2000. Internal growth in access lines has slowed, reflecting the softening of the economy.

TDS Telecom’s competitive local exchange companies served 197,200 access lines at the end of 2001 compared to 112,100 at the end of 2000 and 65,900 at the end of 1999. Internal growth in access lines has increased as CLEC operations have increased their presence in current markets and expanded into new markets.

Year Ended December 31,	2001	2000	1999
(Dollars in thousands)			
<b>Local Telephone Operations</b>			
Operating Revenues			
Local Service	\$179,529	\$168,775	\$152,290
Network access and long-distance	319,410	285,738	269,188
Miscellaneous	77,878	74,468	71,052
	<u>\$576,817</u>	<u>\$528,981</u>	<u>\$492,530</u>
Operating Expenses			
Operating expenses	283,114	261,884	250,994
Depreciation and amortization	131,787	124,389	117,443
	<u>\$414,901</u>	<u>\$386,273</u>	<u>\$368,437</u>
Local Telephone Operating Income	<u>\$161,916</u>	<u>\$142,708</u>	<u>\$124,093</u>
<b>Competitive Local Exchange Operations</b>			
Operating Revenues	\$118,812	\$ 84,720	\$ 55,173
Operating Expenses			
Operating expenses	144,211	90,619	58,808
Depreciation and amortization	17,574	9,056	5,907
	<u>\$161,785</u>	<u>\$99,675</u>	<u>\$64,715</u>
Competitive Local Exchange Operating (Loss)	<u>\$ (42,973)</u>	<u>\$ (14,955)</u>	<u>\$ (9,542)</u>
Intercompany revenue elimination	(1,917)	(3,485)	(1,786)
Intercompany expense elimination	(1,917)	(3,485)	(1,786)
Operating Income	<u>\$118,943</u>	<u>\$127,753</u>	<u>\$114,551</u>
Access lines (ILEC)	650,700	601,200	571,700
Access lines (CLEC)	197,200	112,100	65,900
Growth in ILEC access lines:			
Acquisitions	43,400	10,200	500
Internal growth	6,100	19,300	23,700
Average monthly revenue per ILEC access line	\$ 77.76	\$ 74.75	\$ 73.00
Employees	3,410	2,820	2,590

**Operating Revenues** increased 14% (\$83.5 million) to \$693.7 million in 2001, and 12% (\$64.3 million) to \$610.2 million in 2000. The increase was due to the growth in local telephone operations, including acquisitions, and the expansion of competitive local exchange activities.

## Management’s Discussion and Analysis of Results of Operation and Financial Condition



**Operating Expenses** totaled \$574.8 million in 2001, up 19% (\$92.3 million) from 2000, and totaled \$482.5 million in 2000, up 12% (\$51.1 million) from 1999.

**Operating Income** decreased 7% (\$8.8 million) in 2001 and increased 12% (\$13.2 million) in 2000. TDS Telecom’s overall operating margin was 17.1% in 2001, 20.9% in 2000 and 21.0% in 1999.

### Local Telephone Operations

**Operating revenues** increased 9% (\$47.8 million) to \$576.8 million in 2001 and 7% (\$36.5 million) to \$529.0 million in 2000. Average monthly revenue per local telephone access line was \$77.76 in 2001, \$74.75 in 2000 and \$73.00 in 1999. The majority of the increase in average monthly revenue per local telephone access line in 2001 is related to the increase in long-distance revenues. The increases in all years reflect growth in local service revenues. Local telephone operating revenues are anticipated to continue their pattern of moderate growth.

**Local service revenues** (provision of local telephone exchange service within the franchise serving area of TDS Telecom’s local telephone companies) increased 6% (\$10.8 million) in 2001 and 11% (\$16.5 million) in 2000. Average monthly local service revenue per customer was \$24.20 in 2001, \$23.85 in 2000 and \$22.57 in 1999. Acquisitions increased revenues by \$4.8 million in 2001. Access line growth, excluding acquisitions, of 1.0% in 2001 and 3.4% in 2000, resulted in increases in revenues of \$3.5 million and \$6.7 million, respectively. The sale of custom calling and advanced features increased revenues by \$2.6 million in 2001 and \$4.9 million in 2000.

**Network access and long-distance revenues** (compensation for carrying interstate and intrastate long-distance traffic on TDS Telecom’s local telephone networks) increased 12% (\$33.7 million) in 2001 and 6% (\$16.6 million) in 2000. Average monthly network access and long-distance revenue per customer was \$43.06 in 2001, \$40.38 in 2000 and \$39.90 in 1999. Revenues increased by \$16.3 million in 2001 and \$2.4 million in 2000 as TDS Telecom began selling long-distance service to its customers in the third quarter of 2000. Revenue generated from access minute growth due to increased network usage increased \$7.1 million in 2001 and \$8.3 million in 2000. Acquisitions increased revenues by \$6.5 million in 2001. Compensation from state and national revenue pools due to increased costs of providing network access increased \$4.3 million in 2001 and \$2.3 million in 2000.

**Miscellaneous revenues** (charges for (i) leasing, selling, installing and maintaining customer premise equipment, (ii) providing billing and collection services, (iii) providing Internet services and (iv) selling of digital broadcast satellite receivers) increased 5% (\$3.4 million) in 2001 and 5% (\$3.4 million) in 2000. Average monthly miscellaneous revenue per customer was \$10.50 in 2001, \$10.52 in 2000 and \$10.53 in 1999.

**Operating expenses** increased 7% (\$28.6 million) in 2001 and 5% (\$17.8 million) in 2000. Local telephone expenses as a percent of local telephone revenues were 71.9% in 2001, 73.0% in 2000 and 74.8% in 1999. Local telephone expenses are anticipated to increase due to inflation and new revenue-producing programs and to level off somewhat as a percent of operating revenues.

The increases in local telephone expenses related primarily to the cost of providing Internet service, the sale of long-distance service, acquisitions and wage and benefit increases. TDS Telecom has emphasized cost containment measures to offset rising costs. The sale of long-distance service by TDS Telecom increased expenses by \$10.7 million in 2001 and \$1.7 million in 2000. Acquisitions increased cash expenses by \$10.0 million in 2001. Depreciation and amortization expenses increased 6% (\$7.4 million) in 2001, including \$3.1 million from acquisitions, and 6% (\$6.9 million) in 2000 as a result of increased investment in plant and equipment.

**Operating income** increased 14% (\$19.2 million) to \$161.9 million in 2001 and 15% (\$18.6 million) to \$142.7 million in 2000 from \$124.1 million in 1999. The local telephone operating margin was 28.1% in 2001, 27.0% in 2000 and 25.2% in 1999. The increase in operating margin was caused by the growth in revenue along with the emphasis on controlling costs. Local telephone operating expenses are expected to increase due to inflation while additional revenues and expenses are expected from new or expanded product offerings.