
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2010

or

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

For the transition period from _____ to _____

Commission File No. 001-03040

QWEST CORPORATION

(Exact name of registrant as specified in its charter)

Colorado

(State or other jurisdiction of
incorporation or organization)

1801 California Street, Denver, Colorado

(Address of principal executive offices)

84-0273800

(I.R.S. Employer
Identification No.)

80202

(Zip Code)

(303) 992-1400

(Registrant's telephone number, including area code)

N/A

(Former name, former address and former fiscal year, if changed since last report)

THE REGISTRANT, A WHOLLY OWNED SUBSIDIARY OF QWEST COMMUNICATIONS INTERNATIONAL INC., MEETS THE CONDITIONS SET FORTH IN GENERAL INSTRUCTIONS H(1) (a) AND (b) OF FORM 10-Q AND IS THEREFORE FILING THIS FORM WITH REDUCED DISCLOSURE FORMAT.

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☒ Smaller reporting company ☐
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

On November 2, 2010, one share of Qwest Corporation common stock was outstanding.

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GLOSSARY OF TERMS

Our industry uses many terms and acronyms that may not be familiar to you. To assist you in reading this document and other documents we file with the Securities and Exchange Commission, we have provided below definitions of some of these terms.

- *Access Lines*. Telephone lines reaching from the customer's premises to a connection with the public switched telephone network. Our access lines reported in this document include only those lines used to provide services to external customers and exclude lines used solely by us and our affiliates. We also exclude residential lines that we solely use to provide broadband services.
- *Asynchronous Transfer Mode (ATM)*. A broadband, network transport service utilizing data switches that provides a fast, efficient way to move large quantities of information.
- *Broadband Services (also known as high-speed Internet services)*. Services used to connect to the Internet through existing telephone lines and fiber-optic cables at higher speeds than dial-up access.
- *Competitive Local Exchange Carriers (CLECs)*. Telecommunications providers that compete with us in providing local voice and other services in our local service area, predominantly using our network.
- *Customer Premises Equipment (CPE)*. Telecommunications equipment sold to a customer, usually in connection with our providing telecommunications services to that customer.
- *Data Integration*. Telecommunications equipment located on customers' premises and related professional services. These services include network management, installation and maintenance of data equipment and building of proprietary fiber-optic broadband networks for government and business customers.
- *Dedicated Internet Access (DIA)*. Internet access ranging from 128 kilobits per second to 10 gigabits per second.
- *Facilities expenses*. Third-party telecommunications expenses we incur for using other carriers' networks to provide services to our customers.
- *Fiber to the Cell Site (FTTCS)*. A type of telecommunications network consisting of fiber-optic cables that run from a telecommunication provider's broadband interconnection points to cellular sites. Fiber to the cell site services allow for the delivery of higher bandwidth services supporting mobile technologies than would otherwise generally be available through a more traditional telecommunications network.
- *Fiber to the Node (FTTN)*. A type of telecommunications network that combines fiber-optic cables (which run from a telecommunication provider's central office to a single location within a particular neighborhood or geographic area) and traditional copper wires (which run from this location to individual residences and businesses within the neighborhood or geographic area). Fiber to the node allows for the delivery of higher speed broadband services than would otherwise generally be available through a more traditional telecommunications network made up of only copper wires.
- *Frame Relay*. A high-speed data switching technology used primarily to interconnect multiple local networks.
- *Hosting Services*. The providing of space, power, bandwidth and managed services in data centers.
- *Incumbent Local Exchange Carrier (ILEC)*. A traditional telecommunications provider that, prior to the Telecommunications Act of 1996, had the exclusive right and responsibility for providing local telecommunications services in its local service area. Qwest Corporation is an ILEC.
- *Integrated Services Digital Network (ISDN)*. A telecommunications standard that uses digital transmission technology to support voice, video and data communications applications over regular telephone lines.

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- *Internet Protocol (IP)*. Those protocols that facilitate transferring information in packets of data and that enable each packet in a transmission to “tell” the data switches it encounters where it is headed and enables the computers on each end to confirm that message has been accurately transmitted and received.
- *Managed Services*. Customized, turnkey solutions for integrated data, Internet and voice services offered to business markets customers. These services include a diverse combination of emerging technology products and services, such as VoIP, Ethernet, MPLS, hosting services and advanced voice services, such as web conferencing and call center solutions. Most of these services can be performed from outside our customers’ internal networks, with an emphasis on integrating and certifying Internet security for applications and content.
- *Multi-Protocol Label Switching (MPLS)*. A standards-approved data networking technology that is a substitute for existing frame relay and ATM networks and that can deliver the quality of service required to support real-time voice and video, as well as service level agreements that guarantee bandwidth. MPLS is deployed by many telecommunications providers and large enterprises for use in their own national networks.
- *Private Line*. Direct circuit or channel specifically dedicated to a customer for the purpose of directly connecting two or more sites. Private line offers a high-speed, secure solution for frequent transmission of large amounts of data between sites.
- *Public Switched Telephone Network (PSTN)*. The worldwide voice telephone network that is accessible to every person with a telephone equipped with a dial tone.
- *Unbundled Network Elements (UNEs)*. Discrete elements of our network that are sold or leased to competitive telecommunications providers and that may be combined to provide their retail telecommunications services.
- *Universal Service Funds (USF)*. Federal and state funds established to promote the availability of telecommunications services to all consumers at reasonable and affordable rates, among other things. As a telecommunications provider, we are often required to contribute to these funds.
- *Virtual Private Network (VPN)*. A private network that operates securely within a public network (such as the Internet) by means of encrypting transmissions.
- *Voice over Internet Protocol (VoIP)*. An application that provides real-time, two-way voice communication similar to our traditional voice services that originates in the Internet protocol over a broadband connection and often terminates on the PSTN.
- *Wide Area Network (WAN)*. A communications network that covers a wide geographic area, such as a state or country. A WAN typically extends a local area network outside the building, over telephone common carrier lines to link to other local area networks in remote locations, such as branch offices or at-home workers and telecommuters.

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

QWEST CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	(Dollars in millions)			
Operating revenue:				
Operating revenue	\$ 1,923	\$ 1,995	\$ 5,809	\$ 6,107
Operating revenue—affiliates	388	407	1,162	1,265
Total operating revenue	<u>2,311</u>	<u>2,402</u>	<u>6,971</u>	<u>7,372</u>
Operating expenses:				
Cost of sales (exclusive of depreciation and amortization)	436	435	1,247	1,270
Selling	361	389	1,099	1,258
General, administrative and other operating	377	416	1,154	1,245
Affiliates	51	47	143	129
Depreciation and amortization	470	495	1,402	1,482
Total operating expenses	<u>1,695</u>	<u>1,782</u>	<u>5,045</u>	<u>5,384</u>
Operating income	616	620	1,926	1,988
Other expense (income)—net:				
Interest expense on long-term borrowings—net	150	163	465	471
Other—net	(1)	(16)	(2)	4
Total other expense (income)—net	<u>149</u>	<u>147</u>	<u>463</u>	<u>475</u>
Income before income taxes	467	473	1,463	1,513
Income tax expense	181	180	621	575
Net income	<u>\$ 286</u>	<u>\$ 293</u>	<u>\$ 842</u>	<u>\$ 938</u>

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

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QWEST CORPORATION CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	September 30,	December 31,
	2010	2009
	(Dollars in millions)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 344	\$ 1,014
Accounts receivable—net of allowance of \$47 and \$53, respectively	751	774
Accounts receivable—affiliates	140	71
Deferred income taxes—net	180	167
Prepaid expenses and other	188	245
Total current assets	1,603	2,271
Property, plant and equipment—net	10,193	10,638
Capitalized software—net	891	880
Prepaid pension—affiliate	910	952
Other	251	297
Total assets	<u>\$ 13,848</u>	<u>\$ 15,038</u>
LIABILITIES AND STOCKHOLDER'S (DEFICIT) EQUITY		
Current liabilities:		
Current portion of long-term borrowings	\$ 859	\$ 515
Accounts payable	437	419
Accounts payable—affiliates	90	201
Dividends payable—Qwest Services Corporation	200	100
Accrued expenses and other	925	941
Current portion of post-retirement, other post-employment benefits and other—affiliates	175	176
Deferred revenue and advance billings	379	393
Total current liabilities	3,065	2,745
Long-term borrowings—net of unamortized debt discount and other of \$141 and \$155, respectively	7,099	7,871
Post-retirement, other post-employment benefits and other—affiliates	2,512	2,573
Deferred income taxes—net	1,215	1,127
Other	374	410
Total liabilities	<u>14,265</u>	<u>14,726</u>
Commitments and contingencies (Note 9)		
Stockholder's (deficit) equity:		
Common stock—one share without par value, owned by Qwest Services Corporation	11,373	11,346
Accumulated deficit	(11,790)	(11,034)
Total stockholder's (deficit) equity	<u>(417)</u>	<u>312</u>
Total liabilities and stockholder's (deficit) equity	<u>\$ 13,848</u>	<u>\$ 15,038</u>

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

QWEST CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

	Nine Months Ended September 30,	
	2010	2009
	(Dollars in millions)	
Operating activities:		
Net income	\$ 842	\$ 938
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,402	1,482
Deferred income taxes	55	(70)
Provision for bad debt—net	48	67
Other non-cash charges—net	8	9
Changes in operating assets and liabilities:		
Accounts receivable	(33)	24
Accounts receivable—affiliates	19	61
Prepaid expenses and other current assets	74	11
Accounts payable, accrued expenses and other current liabilities	20	17
Accounts payable, accrued expenses and other current liabilities—affiliates	(189)	(138)
Deferred revenue and advance billings	(20)	(28)
Other non-current assets and liabilities including affiliates	10	70
Cash provided by operating activities	<u>2,236</u>	<u>2,443</u>
Investing activities:		
Expenditures for property, plant and equipment and capitalized software	(919)	(821)
Changes in interest in investments managed by Qwest Services Corporation	29	(1)
Other	1	(6)
Cash used for investing activities	<u>(889)</u>	<u>(828)</u>
Financing activities:		
Proceeds from long-term borrowings	—	738
Repayments of long-term borrowings, including current maturities	(519)	(20)
Dividends paid to Qwest Services Corporation	(1,500)	(1,500)
Other	2	4
Cash used for financing activities	<u>(2,017)</u>	<u>(778)</u>
Cash and cash equivalents:		
(Decrease) increase in cash and cash equivalents	(670)	837
Beginning balance	1,014	233
Ending balance	<u>\$ 344</u>	<u>\$ 1,070</u>

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

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
For the Three and Nine Months Ended September 30, 2010
(Unaudited)

Unless the context requires otherwise, references in this report to “QC” refer to Qwest Corporation, references to “Qwest,” “we,” “us,” the “Company” and “our” refer to Qwest Corporation and its consolidated subsidiaries, references to “QSC” refer to our direct parent company, Qwest Services Corporation, and its consolidated subsidiaries, and references to “QCII” refer to our ultimate parent company, Qwest Communications International Inc., and its consolidated subsidiaries.

Note 1: Basis of Presentation

Our condensed consolidated balance sheet as of December 31, 2009, which was derived from our audited financial statements, and our unaudited interim condensed consolidated financial statements as of and for the three and nine months ended September 30, 2010 have been prepared in accordance with the instructions for Form 10-Q. In compliance with those instructions, certain information and footnote disclosures normally included in consolidated financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted. We believe that the disclosures made are adequate such that the information presented is not misleading.

In the opinion of management, these statements include all normal recurring adjustments necessary to fairly present our condensed consolidated statements of operations, financial position and cash flows as of September 30, 2010 and for all periods presented. Our condensed consolidated statements of operations and condensed consolidated statements of cash flows for the nine months ended September 30, 2010 are not necessarily indicative of the results or cash flows expected for the full year or of the results we would have attained had we operated as a stand-alone entity during the periods presented.

These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2009.

Reclassifications

During the first quarter of 2010, we changed the definitions we use to classify expenses as cost of sales, selling expenses or general, administrative and other operating expenses and, as a result, certain expenses in our condensed consolidated statements of operations for the prior year have been reclassified to conform to the current year presentation. Our new definitions of these expenses are as follows:

- *Cost of sales (exclusive of depreciation and amortization)* are expenses incurred in providing products and services to our customers and affiliates. These expenses include: employee-related expenses directly attributable to operating and maintaining our network (such as salaries, wages and certain benefits); equipment sales expenses (such as modem expenses); rents and utilities expenses incurred by our network operations; fleet expenses; and other expenses directly related to our network operations (such as professional fees and outsourced services).
- *Selling expenses* are expenses incurred in selling products and services to our customers and affiliates. These expenses include: employee-related expenses directly attributable to selling products or services (such as salaries, wages, internal commissions and certain benefits); marketing and advertising; external commissions; bad debt expense; and other selling expenses (such as professional fees and outsourced services).

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
For the Three and Nine Months Ended September 30, 2010
(Unaudited)

Note 1: Basis of Presentation—(Continued)

- *General, administrative and other operating expenses* are corporate overhead and other operating expenses. These expenses include: employee-related expenses for administrative functions (such as salaries, wages and certain benefits); taxes and fees (such as property and other taxes and universal service funds (“USF”) charges); rents and utilities expenses incurred by our administrative offices; and other general, administrative and other operating expenses (such as professional fees). These expenses also include our combined net periodic pension and post-retirement benefits expenses for all eligible employees and retirees allocated to us from QCII.

These definitions reflect changes primarily to reclassify expenses for: rent and utilities incurred by our network operations; fleet; network and supply chain management; and insurance and risk management from general, administrative and other operating expenses to cost of sales, where these expenses are more aligned with how we now manage our business. We believe these changes allow users of our financial statements to better understand our expense structure. These expense classifications may not be comparable to those of other companies. These changes had no impact on total operating expenses or net income for any period. These changes resulted in the reclassification of \$53 million and \$150 million from the general, administrative and other operating expenses and selling expenses categories to cost of sales for the three and nine months ended September 30, 2009, respectively.

Use of Estimates

Our condensed consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles. These accounting principles require us to make certain estimates, judgments and assumptions. We believe that the estimates, judgments and assumptions we made when accounting for items and matters such as, but not limited to, investments, long-term contracts, customer retention patterns, allowance for doubtful accounts, depreciation, amortization, asset valuations, internal labor capitalization rates, affiliate transactions, intercompany allocations, recoverability of assets (including deferred tax assets), impairment assessments, pension, post-retirement and other post-employment benefits, taxes, certain liabilities, and other provisions and contingencies are reasonable, based on information available at the time they were made. These estimates, intercompany allocations, judgments and assumptions can affect the reported amounts of assets, liabilities and components of stockholder’s deficit or equity as of the dates of the condensed consolidated balance sheets, as well as the reported amounts of revenue, expenses and components of cash flows during the periods presented in our condensed consolidated statements of operations and our condensed consolidated statements of cash flows. We also make estimates in our assessments of potential losses in relation to threatened or pending tax and legal matters. See Note 7—Tax Matters and Note 9—Commitments and Contingencies for additional information.

- For matters not related to income taxes, if a loss is considered probable and the amount can be reasonably estimated, we recognize an expense for the estimated loss. If we have the potential to recover a portion of the estimated loss from a third party, we make a separate assessment of recoverability and reduce the estimated loss if recovery is also deemed probable.
- For matters related to income taxes, if the impact of an uncertain tax position is more likely than not to be sustained upon audit by the relevant taxing authority, then we recognize a benefit for the largest amount that is more likely than not to be sustained. No portion of an uncertain tax position will be recognized if the position has less than a 50% likelihood of being sustained. Interest is recognized on the amount of unrecognized benefit from uncertain tax positions.

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
For the Three and Nine Months Ended September 30, 2010
(Unaudited)

Note 1: Basis of Presentation—(Continued)

For all of these and other matters, actual results could differ from our estimates.

USF, Gross Receipts Taxes and Other Surcharges

Our revenue and general, administrative and other operating expenses included taxes and surcharges accounted for on a gross basis of \$45 million and \$144 million for the three and nine months ended September 30, 2010, respectively, and \$48 million and \$137 million for the three and nine months ended September 30, 2009, respectively.

Depreciation and Amortization

Property, plant and equipment is shown net of accumulated depreciation on our condensed consolidated balance sheets. Accumulated depreciation was \$33.808 billion and \$33.022 billion as of September 30, 2010 and December 31, 2009, respectively.

Capitalized software is shown net of accumulated amortization on our condensed consolidated balance sheets. Accumulated amortization was \$1.702 billion and \$1.599 billion as of September 30, 2010 and December 31, 2009, respectively.

QCII-CenturyLink Merger

On April 21, 2010, QCII entered into a merger agreement whereby CenturyLink, Inc. (“CenturyLink”) will acquire QCII in a tax-free, stock-for-stock transaction. Under the terms of the agreement, QCII’s stockholders will receive 0.1664 shares of CenturyLink common stock for each share of QCII’s common stock they own at closing. Based on QCII’s and CenturyLink’s number of outstanding shares as of the date of the merger agreement, at closing CenturyLink shareholders are expected to own approximately 50.5% and QCII’s stockholders are expected to own approximately 49.5% of the combined company. On July 15, 2010, QCII and CenturyLink received notification from the Department of Justice and the Federal Trade Commission that they received early termination of the waiting period under the Hart-Scott-Rodino Act, and as such have clearance from a federal antitrust perspective to proceed with the merger. On August 24, 2010, stockholders of each company approved all proposals relating to the merger. Completion of this transaction remains subject to a number of federal and state regulatory approvals as well as other customary closing conditions. QCII anticipates closing this transaction in the first half of 2011. If the merger agreement is terminated under certain circumstances, QCII may be obligated to pay CenturyLink a termination fee of \$350 million.

Note 2: Fair Value of Financial Instruments

Our financial instruments consist of cash and cash equivalents, auction rate securities, accounts receivable, accounts payable, interest rate hedges and long-term notes including the current portion. The carrying values of the following items approximate their fair values: cash and cash equivalents, auction rate securities, accounts receivable, accounts payable and interest rate hedges. The carrying value of our long-term notes, including the current portion, reflects original cost net of unamortized discounts and other and was \$7.826 billion and \$8.313 billion as of September 30, 2010 and December 31, 2009, respectively. For additional information, see Note 4—Borrowings.

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
For the Three and Nine Months Ended September 30, 2010
(Unaudited)

Note 2: Fair Value of Financial Instruments—(Continued)

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between independent and knowledgeable participants who are willing and able to transact for an asset or liability at the measurement date. We use valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs when determining fair value and then we rank the estimated values based on the reliability of the inputs used following the fair value hierarchy set forth by the Financial Accounting Standards Board (the “FASB”).

The table below presents the fair values for auction rate securities, interest rate hedges and long-term notes including the current portion, as well as the input levels used to determine these fair values as of September 30, 2010 and December 31, 2009:

	<u>Level</u>	<u>Fair Value As Of</u>	
		<u>September 30, 2010</u>	<u>December 31, 2009</u>
(Dollars in millions)			
Assets:			
Auction rate securities	3	\$ 16	\$ 41
Fair value hedges	3	—	2
Total assets		<u>\$ 16</u>	<u>\$ 43</u>
Liabilities:			
Long-term notes, including the current portion	1 & 2	\$ 8,627	\$ 8,495
Cash flow hedges	3	—	3
Total liabilities		<u>\$ 8,627</u>	<u>\$ 8,498</u>

The three levels of the fair value hierarchy as defined by the FASB are as follows:

<u>Input Level</u>	<u>Description of Input</u>
Level 1	Inputs are based upon unadjusted quoted prices for identical instruments traded in active markets.
Level 2	Inputs are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
Level 3	Inputs are generally unobservable and typically reflect management’s estimates of assumptions that market participants would use in pricing the asset or liability. The fair values are therefore determined using model-based techniques that include option pricing models, discounted cash flow models, and similar techniques.

We determined the fair value of our auction rate securities using a probability-weighted discounted cash flow model that takes into consideration the weighted average of the following factors:

- coupon rate of 4.57%;
- probability that we will be able to sell the securities in an auction or that the securities will be redeemed early of 76.30%;

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
For the Three and Nine Months Ended September 30, 2010
(Unaudited)

Note 2: Fair Value of Financial Instruments—(Continued)

- probability that a default will occur of 20.27% with a related recovery rate of 55.00%; and
- discount rate of 7.15%.

We determined the fair value of our interest rate hedges using projected future cash flows, discounted at the mid-market implied forward London Interbank Offered Rates (“LIBOR”) associated with those cash flows. We determined this valuation excluding accrued interest. For additional information on our derivative financial instruments, see Note 5—Derivative Financial Instruments.

We determined the fair values of our long-term notes including the current portion based on quoted market prices where available or, if not available, based on future cash flows discounted using current market interest rates.

The table below presents a rollforward of the instruments valued using Level 3 inputs for the nine months ended September 30, 2010:

	Instruments Valued Using Level 3 Inputs		
	Auction Rate	Fair Value	Cash Flow
	Securities	Hedges (Dollars in millions)	Hedges
Balance at December 31, 2009	\$ 41	\$ 2	\$ (3)
Transfers into (out of) Level 3	—	—	—
Additions	—	—	—
Dispositions and settlements	(30)	(7)	—
Realized and unrealized (losses) gains:			
Included in long-term borrowings—net	—	5	—
Included in other income (expense)—net	—	—	—
Included in other comprehensive (loss) income	5	—	3
Balance at September 30, 2010	<u>\$ 16</u>	<u>\$ —</u>	<u>\$ —</u>

Note 3: Investments

QSC manages the majority of our cash and investments. Our proportionate ownership of these investments, including illiquid investments, can change because we record our portion of the entire portfolio of cash and investments managed by QSC. Our allocated portion changes as our cash balances change compared to the cash balances of our affiliate companies. These changes are reflected on a net basis in cash flows from investing activities on our condensed consolidated statements of cash flows.

As of September 30, 2010, our investments included auction rate securities, which are classified as non-current, available-for-sale investments and are included in other non-current assets at their estimated fair value on our condensed consolidated balance sheets.

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
For the Three and Nine Months Ended September 30, 2010
(Unaudited)

Note 3: Investments—(Continued)

The following table summarizes our unrealized gain (loss), net of deferred income taxes, due to the change in the amount of auction rate securities allocated to us by QSC:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	(Dollars in millions)			
Unrealized gain (loss), net of deferred income taxes	\$ —	\$ —	\$ 3	\$ (1)

The following table summarizes our balance of these auction rate securities, the cumulative net unrealized loss, net of deferred income taxes, related to these securities and the cost basis of these securities:

	September 30,		December 31,	
	2010	2009	2010	2009
	(Dollars in millions)			
Auction rate securities—fair value	\$ 16	\$ 41		
Classification				
		Non-current, available-for-sale investments		
Balance sheet location (reported at estimated fair value)		Other non-current assets		
Cumulative net unrealized loss, net of deferred income taxes	\$ 3	\$ 6		
Auction rate securities—cost basis	\$ 21	\$ 51		

These unrealized losses were recorded in accumulated other comprehensive income, which is included in accumulated deficit in our condensed consolidated balance sheets. We consider the decline in fair value to be a temporary impairment because we believe it is more likely than not that we will ultimately recover the entire \$21 million cost basis, in part because the securities are rated investment grade, the securities are collateralized and the issuers continue to make required interest payments. Prior to August 2007, QSC invested in these securities for short periods of time as part of its cash management program. However, the state of the credit markets has prevented QSC and other investors from liquidating holdings of these securities in auctions since the third quarter of 2007. At some point in the future, we may determine that the decline in fair value is other than temporary if, among other factors:

- the issuers cease making required interest payments;
- we believe it is more likely than not that we will be required to sell these securities before their values recover; or
- we change our intent to hold the securities due to events such as a change in the terms of the securities.

Our auction rate securities have stated maturities between 2033 and 2036.

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
For the Three and Nine Months Ended September 30, 2010
(Unaudited)

Note 4: Borrowings

As of September 30, 2010 and December 31, 2009, our long-term borrowings, net of unamortized discounts and other, consisted of the following:

	September 30,	December 31,
	2010	2009
	(Dollars in millions)	
Current portion of long-term borrowings:		
Long-term notes	\$ 825	\$ 500
Long-term capital lease and other obligations	34	15
Total current portion of long-term borrowings	859	515
Long-term borrowings—net:		
Long-term notes—net	7,001	7,813
Long-term capital lease and other obligations—net	98	58
Total long-term borrowings—net	7,099	7,871
Total borrowings—net	<u>\$ 7,958</u>	<u>\$ 8,386</u>

We were in compliance with all provisions and covenants of our borrowings as of September 30, 2010.

Repayment

In June 2010, we paid at maturity the \$500 million aggregate principal amount of our 6.95% Term Loan due 2010.

Credit Facility

QCII's revolving credit facility (the "Credit Facility"), which makes available to QCII \$1.035 billion of additional credit subject to certain restrictions, is currently undrawn and expires in September 2013; however, the Credit Facility will be terminated or amended at the time of the closing of QCII's merger with CenturyLink. The Credit Facility has 13 lenders, with commitments ranging from \$25 million to \$100 million. Any amounts drawn on the Credit Facility by QCII are guaranteed by QSC and are secured by a senior lien on our stock.

Note 5: Derivative Financial Instruments

We sometimes use derivative financial instruments, specifically interest rate swap contracts, to manage interest rate risks. We execute these instruments with financial institutions we deem creditworthy and monitor our exposure to these counterparties. An interest rate hedge is generally designated as either a cash flow hedge or a fair value hedge. In a cash flow hedge, a borrower of variable interest debt agrees with another party to make fixed payments equivalent to paying fixed rate interest on debt in exchange for receiving payments from the other party equivalent to receiving variable rate interest on debt, the effect of which is to eliminate some portion of the variability in the borrower's overall cash flows. In a fair value hedge, a borrower of fixed rate debt agrees

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
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Note 5: Derivative Financial Instruments—(Continued)

with another party to make variable payments equivalent to paying variable rate interest on the debt in exchange for receiving fixed payments from the other party equivalent to receiving fixed rate interest on debt, the effect of which is to eliminate some portion of the variability in the fair value of the borrower's overall debt portfolio due to changes in interest rates.

We recognize all derivatives on our condensed consolidated balance sheets at fair value. We generally designate the derivative as either a cash flow hedge or a fair value hedge on the date on which we enter into the derivative instrument. Cash flows from derivative instruments that are cash flow hedges or fair value hedges are classified in cash flows from operations.

For a derivative that is designated as and meets all of the required criteria for a cash flow hedge, we record in accumulated other comprehensive income, which is included in accumulated deficit in our condensed consolidated balance sheets, any changes in the fair value of the derivative. We then reclassify these amounts into earnings as the underlying hedged item affects earnings. In addition, if there are any changes in the fair value of the derivative arising from ineffectiveness of the cash flow hedging relationship, we record those amounts immediately in other expense (income)—net in our condensed consolidated statements of operations. For a derivative that is designated as and meets all of the required criteria for a fair value hedge, we record in other expense (income)—net in our condensed consolidated statements of operations the changes in fair value of the derivative and the underlying hedged item. However, if the terms of this type of derivative match the terms of the underlying hedged item such that we qualify to assume no ineffectiveness, then the fair value of the derivative is measured and the change in the fair value for the period is assumed to equal the change in the fair value of the underlying hedged item for the period, with no impact in other expense (income)—net.

We assess quarterly whether each derivative is highly effective in offsetting changes in fair values or cash flows of the hedged item or whether our initial assumption of no ineffectiveness is still valid. If we determine that a derivative is not highly effective as a hedge, a derivative has ceased to be a highly effective hedge or our assumption of no ineffectiveness is no longer valid, then we discontinue hedge accounting with respect to that derivative prospectively. We record immediately in earnings changes in the fair value of derivatives that are not designated as hedges.

Interest Rate Hedges

During 2009 and 2008, we entered into the interest rate hedges described below as part of our short-term and long-term debt strategies.

In August 2009, we entered into interest rate hedges on \$400 million of the outstanding \$1.500 billion aggregate principal amount of our 8.875% Notes due in 2012. We designated these interest rate hedges as fair value hedges. We terminated these interest rate hedges in the third quarter of 2010. Upon termination, we received \$10 million in cash for the fair value of the hedges and accrued interest. The accumulated \$7 million increase in the carrying value of the notes is being amortized to interest expense using the effective interest method over the remaining term of the notes.

In March 2008, we entered into interest rate hedges on \$500 million of the outstanding \$750 million aggregate principal amount of our Floating Rate Notes due 2013. We designated these interest rate hedges as cash flow hedges. These hedges expired in March 2010. We did not recognize any gain or loss in earnings for hedge ineffectiveness during the lives of the hedges.

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
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Note 5: Derivative Financial Instruments—(Continued)

As of September 30, 2010, we had no outstanding interest rate hedge contracts. The interest rate hedges that were previously outstanding had immaterial effects on our consolidated statements of operations and balance sheets in all periods presented.

Note 6: Severance

For the three months ended September 30, 2010 and 2009, we recorded severance expenses of \$40 million and \$11 million, respectively. For the nine months ended September 30, 2010 and 2009, we recorded severance expenses of \$49 million and \$54 million, respectively. A portion of our severance expenses is included in each of cost of sales, selling expenses and general, administrative and other operating expenses in our condensed consolidated statements of operations. As of September 30, 2010 and December 31, 2009, our severance liability was \$47 million and \$75 million, respectively, and is included in accrued expenses and other in our condensed consolidated balance sheets.

Note 7: Tax Matters

During the nine months ended September 30, 2010, our income tax expense increased by \$55 million as a result of the March 2010 enactments of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010. Among other things, these laws disallow, beginning in 2013, federal income tax deductions for retiree prescription drug benefits to the extent we receive reimbursements for those benefits under the Medicare Part D program. Although this tax increase does not take effect until 2013, under accounting principles generally accepted in the U.S. we recognize the full accounting impact in the period in which the laws are enacted.

During the nine months ended September 30, 2010, we reduced our unrecognized tax benefits to zero, a decrease of \$13 million due to settlements with taxing authorities.

Note 8: Contribution to QCII Segments

Our operations are integrated into and are part of the segments of QCII. Our business contributes to all three of QCII's segments: business markets, mass markets and wholesale markets. QCII's Chief Operating Decision Maker ("CODM"), who is also our CODM, reviews our financial information only in connection with our quarterly and annual reports that we file with the Securities and Exchange Commission ("SEC"). Consequently, we do not provide our discrete financial information to the CODM on a regular basis.

Revenue from our products and services for the three and nine months ended September 30, 2010 and 2009 is summarized in the following table:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
	(Dollars in millions)			
Operating revenue by category:				
Strategic services ⁽¹⁾	\$ 774	\$ 722	\$2,281	\$2,164
Legacy services ⁽²⁾	1,104	1,227	3,385	3,809
Affiliates and other services ⁽³⁾	433	453	1,305	1,399
Total operating revenue	<u>\$ 2,311</u>	<u>\$ 2,402</u>	<u>\$6,971</u>	<u>\$7,372</u>

QWEST CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
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Note 8: Contribution to QCII Segments—(Continued)

- (1) Our strategic services include primarily private line, broadband, video and Verizon Wireless services.
- (2) Our legacy services include primarily local, access, integrated services digital network (“ISDN”) and traditional wide area network (“WAN”) services.
- (3) Our affiliates and other services consist primarily of services we provide to our affiliates and USF surcharges. We provide to our affiliates: data, local services and billing and collections services that we also provide to external customers. In addition, we provide to our affiliates: marketing, sales and advertising; computer system development and support services; network support and technical services; and other support services, such as legal, regulatory, finance and accounting, tax, human resources and executive support.

Note 9: Commitments and Contingencies

QCII is involved in several legal proceedings to which we are not a party that, if resolved against QCII, could have a material adverse effect on our business and financial condition. We have included below a discussion of these matters. Only those matters to which we are a party represent contingencies for which we have accrued, or could reasonably anticipate accruing, liabilities if appropriate to do so. We are not a party to any of the matters discussed below and therefore have not accrued any liabilities for these matters.

In this section, when we refer to a class action as “putative” it is because a class has been alleged, but not certified in that matter. Until and unless a class has been certified by the court, it has not been established that the named plaintiffs represent the class of plaintiffs they purport to represent.

The terms and conditions of applicable bylaws, certificates or articles of incorporation, agreements or applicable law may obligate QCII to indemnify its former directors, officers or employees with respect to certain of the matters described below, and QCII has been advancing legal fees and costs to certain former directors, officers or employees in connection with certain matters described below.

KPNQwest Litigation/Investigation

On September 29, 2010, the trustees in the Dutch bankruptcy proceeding for KPNQwest, N.V. (of which QCII was a major shareholder) filed a lawsuit in district court in Haarlem, the Netherlands, alleging tort and mismanagement claims under Dutch law. QCII and Koninklijke KPN N.V. (“KPN”) are defendants in this lawsuit along with a number of former KPNQwest supervisory board members and a former officer of KPNQwest, some of whom were formerly affiliated with QCII. Plaintiffs allege, among other things, that defendants’ actions were a cause of the bankruptcy of KPNQwest, and they seek damages for the bankruptcy deficit of KPNQwest, which is claimed to be approximately €4.2 billion (or approximately \$5.7 billion based on the exchange rate on September 30, 2010), plus statutory interest. Two lawsuits asserting similar claims were previously filed against QCII and others in federal courts in New Jersey and Colorado, from which they were dismissed without prejudice on the ground that the claims should not be litigated in the United States.

On September 13, 2006, Cargill Financial Markets, Plc and Citibank, N.A. filed a lawsuit in the District Court of Amsterdam, the Netherlands, against QCII, KPN, KPN Telecom B.V., and other former officers, employees or supervisory board members of KPNQwest, some of whom were formerly affiliated with QCII. The lawsuit alleges that defendants misrepresented KPNQwest’s financial and business condition in connection with

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Note 9: Commitments and Contingencies—(Continued)

the origination of a credit facility and wrongfully allowed KPNQwest to borrow funds under that facility. Plaintiffs allege damages of approximately €219 million (or approximately \$300 million based on the exchange rate on September 30, 2010).

On October 31, 2002, Richard and Marcia Grand, co-trustees of the R.M. Grand Revocable Living Trust, dated January 25, 1991, filed a lawsuit in Arizona Superior Court. As amended and following the appeal of a partial summary judgment against plaintiffs which was affirmed in part and reversed in part, plaintiffs' complaint alleges, among other things, that defendants violated state securities laws in connection with plaintiffs' investments in KPNQwest securities. QCII was a defendant in this lawsuit along with Qwest B.V. (one of QCII's subsidiaries), Joseph P. Nacchio, QCII's former chief executive officer, and John McMaster, the former president and chief executive officer of KPNQwest. The Arizona Superior Court dismissed most of plaintiffs' claims, and plaintiffs voluntarily dismissed the remainder of their claims. Plaintiffs appealed the court's decision to the Arizona Court of Appeals, which affirmed the Arizona Superior Court's decision. The Arizona Supreme Court granted plaintiffs' petition for review, and affirmed the decision by the Arizona Court of Appeals. Plaintiffs claimed to have lost approximately \$9 million in their investments in KPNQwest and were also seeking interest and attorneys' fees.

On August 23, 2005, the Dutch Shareholders Association (Vereniging van Effectenbezitters, or VEB) filed a petition for inquiry with the Enterprise Chamber of the Amsterdam Court of Appeals, the Netherlands, with regard to KPNQwest. VEB sought an inquiry into the policies and course of business at KPNQwest that are alleged to have caused the bankruptcy of KPNQwest in May 2002, and an investigation into alleged mismanagement of KPNQwest by its executive management, supervisory board members, joint venture entities (QCII and KPN), and KPNQwest's outside auditors and accountants. On December 28, 2006, the Enterprise Chamber ordered an inquiry into the management and conduct of affairs of KPNQwest for the period January 1 through May 23, 2002. On December 5, 2008, the Enterprise Chamber appointed investigators to conduct the inquiry. VEB claims that certain individuals have assigned to it their claims for losses totaling approximately €40 million (or approximately \$55 million based on the exchange rate on September 30, 2010), which those individuals allegedly incurred on investments in KPNQwest securities. VEB has not yet filed any adjudicative action to assert those claims.

On June 7, 2010, a number of parties, including QCII and KPN, reached a settlement with VEB for €19 million (or approximately \$25 million based on the exchange rate on September 30, 2010), conditioned in part on the termination of the investigation by the Enterprise Chamber. Pursuant to the terms of the settlement, VEB formally requested that the Enterprise Chamber terminate the investigation. The Enterprise Chamber denied that request and directed the investigation to proceed. The Enterprise Chamber's decision has been appealed to the Dutch Supreme Court.

QCII will continue to defend against the pending KPNQwest litigation matters vigorously.

QCII Stockholder Litigation

In the weeks following the April 22, 2010 announcement of QCII's pending merger with CenturyLink, purported QCII stockholders filed 17 lawsuits against QCII, its directors, certain of its officers, CenturyLink and SB44 Acquisition Company. The purported stockholder plaintiffs commenced these actions in three jurisdictions: the District Court for the City and County of Denver, the United States District Court for the District of Colorado, and the Delaware Court of Chancery. The plaintiffs generally allege that QCII's directors breached

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Note 9: Commitments and Contingencies—(Continued)

their fiduciary duties in approving the merger and seek to enjoin the merger and, in some cases, damages if the merger is completed. Many of the lawsuits also challenge the sufficiency of the disclosures in the preliminary joint proxy statement-prospectus relating to the merger, which was filed with the SEC on June 4, 2010.

QCII, and its directors, believe that all of these actions are without merit. The defendants nevertheless negotiated with the purported stockholder plaintiffs regarding a settlement of the claims asserted in all of these actions, including the claims that challenge the sufficiency of the disclosures in the preliminary joint proxy statement-prospectus. On July 16, 2010, the parties entered into a memorandum of understanding reflecting the terms of their agreement-in-principle for a settlement of all of the claims asserted in these actions. Pursuant to this agreement, defendants included additional disclosures in the final joint proxy statement-prospectus filed with the SEC on July 19, 2010. If the settlement is consummated, all of these actions will be dismissed, with prejudice. The defendants intend to defend their positions in these matters vigorously to the extent they are not fully resolved by the settlement.

Other Matters

Several putative class actions relating to the installation of fiber-optic cable in certain rights-of-way were filed against several other subsidiaries of QCII on behalf of landowners on various dates and in various courts in Arizona, California, Colorado, Georgia, Illinois, Indiana, Kansas, Massachusetts, Mississippi, Missouri, Nevada, New Mexico, Oregon, South Carolina, Tennessee, Texas and Utah. For the most part, the complaints challenge the right to install fiber-optic cable in railroad rights-of-way. The complaints allege that the railroads own the right-of-way as an easement that did not include the right to permit the defendants to install fiber-optic cable in the right-of-way without the plaintiffs' consent. Most of the actions purport to be brought on behalf of state-wide classes in the named plaintiffs' respective states, although two of the currently pending actions purport to be brought on behalf of multi-state classes. Specifically, the Illinois state court action purports to be on behalf of landowners in Illinois, Iowa, Kentucky, Michigan, Minnesota, Nebraska, Ohio and Wisconsin, and the Indiana state court action purports to be on behalf of a national class of landowners. In general, the complaints seek damages on theories of trespass and unjust enrichment, as well as punitive damages. On July 18, 2008, a federal district court in Massachusetts entered an order preliminarily approving a settlement of all of the actions described above, except the action pending in Tennessee. On September 10, 2009, the court denied final approval of the settlement on grounds that it lacked subject matter jurisdiction. On December 9, 2009, the court issued a revised ruling that, among other things, denied a motion for approval as moot and dismissed the matter for lack of subject matter jurisdiction.

One of QCII's other subsidiaries, Qwest Communications Company, LLC ("QCC"), is a defendant in litigation filed by several billing agents for the owners of payphones seeking compensation for coinless calls made from payphones. The matter is pending in the United States District Court for the District of Columbia. Generally, the payphone owners claim that QCC underpaid the amount of compensation due to them under Federal Communications Commission regulations for coinless calls placed from their phones onto QCC's network. The claim seeks compensation for calls, as well as interest and attorneys' fees. QCC will vigorously defend against this action.

A putative class action filed on behalf of certain of QCII's retirees was brought against QCII, the Qwest Group Life Insurance Plan and other related entities in federal district court in Colorado in connection with QCII's decision to reduce the life insurance benefit for these retirees to a \$10,000 benefit. The action was filed on March 30, 2007. The plaintiffs allege, among other things, that QCII and other defendants were obligated to

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Note 9: Commitments and Contingencies—(Continued)

continue their life insurance benefit at the levels in place before QCII decided to reduce them. Plaintiffs seek restoration of the life insurance benefit to previous levels and certain equitable relief. The district court ruled in QCII's favor on the central issue of whether QCII properly reserved our right to reduce the life insurance benefit under applicable law and plan documents. The plaintiffs subsequently amended their complaint to assert additional claims. In 2009, the court dismissed or granted summary judgment to QCII on all of the plaintiffs' claims. The plaintiffs have appealed the court's decision to the Tenth Circuit Court of Appeals.

QCII continues to evaluate the method it uses to assess the amount of USF payments that must be made on certain products, and during the three months ended September 30, 2010, QCII recorded an adjustment to its liability of \$15 million related to previous years' USF payments. This ongoing evaluation may result in further adjustments to QCII's previous years' USF payments and charges to customers.

Note 10: Dividends

Our Board of Directors declared the following cash dividends to QSC in 2010:

<u>Date Declared</u>	<u>Total Amount</u> (Dollars in millions)
March 10, 2010	\$ 400
April 14, 2010	\$ 800
August 18, 2010	\$ 400
October 20, 2010	\$ 700

During the three and nine months ended September 30, 2010, we paid cash dividends to QSC of \$500 million and \$1.500 billion, respectively.

The timing of cash payments for declared dividends to QSC is at our discretion in consultation with QSC. We may continue to declare and pay dividends to QSC in excess of our earnings to the extent permitted by applicable law. Our debt covenants do not limit the amount of dividends we can pay to QSC.

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

Unless the context requires otherwise, references in this report to “QC” refer to Qwest Corporation, references to “Qwest,” “we,” “us,” the “Company” and “our” refer to Qwest Corporation and its consolidated subsidiaries, references to “QSC” refer to our direct parent company, Qwest Services Corporation, and its consolidated subsidiaries, and references to “QCII” refer to our ultimate parent company, Qwest Communications International Inc., and its consolidated subsidiaries.

Certain statements in this report constitute forward-looking statements. See “Special Note Regarding Forward-Looking Statements” at the end of this Item 2 for additional factors relating to these statements, and see “Risk Factors” in Item 1A of Part II of this report for a discussion of certain risk factors applicable to our business, financial condition and results of operations.

Business Overview and Presentation

We offer data, Internet, video and voice services within the 14-state region of Arizona, Colorado, Idaho, Iowa, Minnesota, Montana, Nebraska, New Mexico, North Dakota, Oregon, South Dakota, Utah, Washington and Wyoming. We refer to this region as our local service area.

On April 21, 2010, QCII entered into a merger agreement whereby CenturyLink, Inc. (“CenturyLink”) will acquire QCII in a tax-free, stock-for-stock transaction. Under the terms of the agreement, QCII’s stockholders will receive 0.1664 shares of CenturyLink common stock for each share of QCII’s common stock they own at closing. Based on QCII’s and CenturyLink’s number of outstanding shares as of the date of the merger agreement, at closing CenturyLink shareholders are expected to own approximately 50.5% and QCII’s stockholders are expected to own approximately 49.5% of the combined company. On July 15, 2010, QCII and CenturyLink received notification from the Department of Justice and the Federal Trade Commission that they received early termination of the waiting period under the Hart-Scott-Rodino Act, and as such have clearance from a federal antitrust perspective to proceed with the merger. On August 24, 2010, stockholders of each company approved all proposals relating to the merger. Completion of this transaction remains subject to a number of federal and state regulatory approvals as well as other customary closing conditions. QCII anticipates closing this transaction in the first half of 2011. If the merger agreement is terminated under certain circumstances, QCII may be obligated to pay CenturyLink a termination fee of \$350 million.

Our operations are included in the consolidated operations of QCII and generally account for the majority of QCII’s consolidated revenue. In addition to our operations, QCII maintains a national telecommunications network. Through its fiber optic network, QCII provides the following products and services that we do not provide:

- Data integration;
- Dedicated Internet access;
- Hosting services;
- Long-distance services that allow calls that cross telecommunications geographical areas;
- Managed services;
- Multi-protocol label switching; and
- Voice over Internet Protocol, or VoIP.

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During the first quarter of 2010, we changed the definitions we use to classify expenses as cost of sales, selling expenses or general, administrative and other operating expenses and, as a result, certain expenses in our condensed consolidated statements of operations for the prior year have been reclassified to conform to the current year presentation. Our new definitions of these expenses are as follows:

- *Cost of sales (exclusive of depreciation and amortization)* are expenses incurred in providing products and services to our customers and affiliates. These expenses include: employee-related expenses directly attributable to operating and maintaining our network (such as salaries, wages and certain benefits); equipment sales expenses (such as modem expenses); rents and utilities expenses incurred by our network operations; fleet expenses; and other expenses directly related to our network operations (such as professional fees and outsourced services).
- *Selling expenses* are expenses incurred in selling products and services to our customers and affiliates. These expenses include: employee-related expenses directly attributable to selling products or services (such as salaries, wages, internal commissions and certain benefits); marketing and advertising; external commissions; bad debt expense; and other selling expenses (such as professional fees and outsourced services).
- *General, administrative and other operating expenses* are corporate overhead and other operating expenses. These expenses include: employee-related expenses for administrative functions (such as salaries, wages and certain benefits); taxes and fees (such as property and other taxes and universal service funds, or USF, charges); rents and utilities expenses incurred by our administrative offices; and other general, administrative and other operating expenses (such as professional fees). These expenses also include our combined net periodic pension and post-retirement benefits expenses for all eligible employees and retirees allocated to us from QCII.

These definitions reflect changes primarily to reclassify expenses for: rent and utilities incurred by our network operations; fleet; network and supply chain management; and insurance and risk management from general, administrative and other operating expenses to cost of sales, where these expenses are more aligned with how we now manage our business. We believe these changes allow users of our financial statements to better understand our expense structure. These expense classifications may not be comparable to those of other companies. These changes had no impact on total operating expenses or net income for any period. These changes resulted in the reclassification of \$53 million and \$150 million from the general, administrative and other operating expenses and selling expenses categories to cost of sales for the three and nine months ended September 30, 2009, respectively.

During the first quarter of 2010 we updated our methodology for counting our subscribers and access lines where we provide the services. We now count broadband subscribers and access lines when we earn revenue associated with them. Our access line methodology includes only those access lines that we use to provide services to external customers and excludes lines used solely by us and our affiliates and residential lines that we solely use to provide broadband services. Our new broadband methodology also excludes business and wholesale markets customers from our broadband subscribers.

During the first quarter of 2010 we also updated our methodology for counting our partnership based video subscribers. We now count these subscribers when we earn revenue associated with them, regardless of whether we actually bill the subscribers for the services. Beginning in mid-2009 we began to earn an ongoing commission associated with video customers that we no longer bill so long as they remain active customers of DIRECTV. Because of the change in this commission we have begun to include them in our subscriber counts. This methodology change has increased our video subscribers by approximately 57,000 at the end of the first quarter of 2010, an additional 3,000 subscribers at the end of the second quarter of 2010 and an additional 4,000 subscribers at the end of the third quarter of 2010. We believe the methodology updates described above align our subscribers and access lines with our revenue and better reflect our ongoing operations.

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We have restated our subscribers and access lines reported as of September 30, 2009 to conform to the current period presentation. The table below quantifies these changes by segment:

	September 30, 2009			
	Business Markets	Wholesale		Total
		Mass Markets (in thousands)	Markets	
Previously reported access lines	2,468	7,045	1,048	10,561
Affiliates and us	(442)	—	—	(442)
Alignment to billed units	10	13	28	51
Currently reported access lines	<u>2,036</u>	<u>7,058</u>	<u>1,076</u>	<u>10,170</u>
Previously reported broadband subscribers	—	2,931	—	2,931
Excluding business and wholesale customers	—	(146)	—	(146)
Alignment to billed units	—	(42)	—	(42)
Currently reported broadband subscribers	<u>—</u>	<u>2,743</u>	<u>—</u>	<u>2,743</u>
Previously reported video subscribers	—	849	—	849
Alignment to billed units	—	39	—	39
Currently reported video subscribers	<u>—</u>	<u>888</u>	<u>—</u>	<u>888</u>

For certain products and services we provide, and for a variety of internal communications functions, we use parts of QCII's telecommunications network to transport voice and data traffic. Through its network, QCII also provides nationally and globally some data and Internet access services that are similar to services we provide within our local service area. These services include private line, and our traditional wide area network, or WAN, services, which consist of asynchronous transfer mode, or ATM, and frame relay.

Our operations are integrated into and are part of the segments of QCII and contribute to all three of QCII's segments: business markets, mass markets and wholesale markets. We currently group our products and services among the following three categories:

- *Strategic services*, which include primarily private line, broadband, video and Verizon Wireless services;
- *Legacy services*, which include primarily local, access, integrated services digital network, or ISDN, and traditional wide area network, or WAN, services; and
- *Affiliates and other services*, consisting primarily of services we provide to our affiliates and USF surcharges. We provide to our affiliates data, local services and billing and collections services that we also provide to external customers. In addition, we provide to our affiliates: marketing, sales and advertising; computer system development and support services; network support and technical services; and other support services, such as legal, regulatory, finance and accounting, tax, human resources and executive support.

We have reclassified certain prior year expense, access line and subscriber amounts presented in our Quarterly Report on Form 10-Q for the three months ended September 30, 2009 to conform to the current period presentation.

Our analysis presented below is organized to provide the information we believe will be useful for understanding the relevant trends affecting our business. This discussion should be read in conjunction with our condensed consolidated financial statements and the notes thereto in Item 1 of Part I of this report. Unless otherwise noted below, discussions related to changes in revenue and expenses are applicable to both the three and nine months ended September 30, 2010.

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Business Trends

Our financial results were impacted by several significant trends, which are described below. We expect that these trends will continue to affect our results of operations, cash flows or financial position.

- *Strategic services.* We continue to see shifts in the makeup of our total revenue as customers move to strategic services, such as private line, broadband and video services, from legacy services, such as local and access services. Revenue from our strategic services represented 33% and 30% of our total revenue for the three months ended September 30, 2010 and 2009, respectively, and 33% and 29% of our total revenue for the nine months ended September 30, 2010 and 2009, respectively, and this percentage continues to grow. With respect to broadband services, we continue to focus on increasing subscribers, particularly among consumer and small business customers. We reached approximately 2.9 million broadband subscribers at September 30, 2010 compared to approximately 2.7 million at September 30, 2009. We believe the ability to continually increase connection speeds is competitively important. As a result, we continue to invest in our fiber to the node, or FTTN, deployment, which we launched to meet customer demand for higher broadband speeds. In addition to the FTTN deployment, we continue to expand our product offerings and enhance our marketing efforts as we compete in a competitive and maturing market in which a significant portion of consumers already have broadband services. We expect these efforts will improve our ability to compete and grow our broadband subscribers. Demand for the private line services we offer to business and wholesale customers continues to increase, although our customers' optimization of their networks and industry consolidation have negatively impacted our private line revenue. While we expect that these factors will continue to impact our business, we also believe our fiber strategy will favorably influence our private line revenue through increased demand.
- *Legacy services.* Revenue from our legacy services represented 48% and 51% of our total revenue for the three months ended September 30, 2010 and 2009, respectively, and 49% and 52% of our total revenue for the nine months ended September 30, 2010 and 2009, respectively, and continues to decline. Our legacy services revenue has been, and we expect it will continue to be, adversely affected by access line losses. Intense competition and product substitution continue to drive our access line losses. For example, many consumers are substituting cable and wireless for traditional voice telecommunications services. This has increased the number and type of competitors within our industry and has decreased our market share. We expect that these factors will continue to impact our business. Product bundling and other product promotions, as described below, continue to be some of our responses to offset the loss of revenue as a result of access line losses. We are also experiencing price compression relating to some of our legacy services offered to our enterprise and government customers.
- *Product bundling and product promotions.* We offer our customers, primarily consumers and small businesses, the ability to bundle multiple products and services. For example, through joint marketing and advertising efforts with our affiliates, these customers can bundle local services with other services such as broadband, video, long-distance and wireless. While video and wireless subscribers are an important piece of our customer retention strategy, they do not make a large contribution to strategic services revenue. We believe customers value the convenience of, and price discounts associated with, receiving multiple services through a single company. In addition to our bundle discounts, we also offer limited time promotions on our broadband service for qualifying customers who have our broadband product in their bundle, which we believe will positively affect our acquisition volume and drive customers to purchase more expanded offerings. While bundle price discounts have resulted in lower average revenue for our individual products, we believe product bundles continue to positively impact our customer retention.
- *Operating efficiencies.* We continue to evaluate our operating structure and focus. This involves balancing our workforce in response to our workload, productivity improvements, changes in the telecommunications industry and governmental regulations. Through planned reductions and normal

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employee attrition, we have reduced our workforce and employee-related expenses (net of severance) while achieving operational efficiencies and improving processes through automation and other innovative ways of operating our business.

- *Pension and post-retirement benefits expenses.* QCII is required to recognize on its consolidated financial statements certain expenses relating to its pension and post-retirement health care and life insurance benefits plans. These expenses are calculated based on several assumptions, including among other things discount rates and expected rates of return on plan assets that are set at December 31 of each year. Changes in these assumptions can cause significant changes in the combined net periodic benefits expenses QCII recognizes. QCII allocates the expenses of these plans to us and its other affiliates. The allocation of expenses to us is based upon the demographics of our employees and retirees compared to all the remaining participants. Changes in QCII's assumptions can cause significant changes in the net periodic pension and post-retirement benefits expenses we recognize.
- *Disciplined capital expenditures.* Our capital expenditures continue to be focused on our strategic services such as broadband. For the remainder of 2010, we anticipate that our fiber investment, which includes fiber to the cell site, or FTTCS, will continue to remain an important piece of our capital outlay. Our fiber strategy is the largest contributor to our projected capital expenditures for 2010 increasing to \$1.4 billion or less. In addition, we continue to use lease financing in 2010 for some portion of our capital spending.

While these trends are important to understanding and evaluating our financial results, the other transactions, events and trends discussed in "Risk Factors" in Item 1A of Part II of this report may also materially impact our business operations and financial results.

Results of Operations

Overview

The following table summarizes our results of operations for the three and nine months ended September 30, 2010 and 2009 and the number of employees as of September 30, 2010 and 2009:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2010	2009	Increase/ (Decrease)	% Change	2010	2009	Increase/ (Decrease)	% Change
	(Dollars in millions)							
Operating revenue	\$2,311	\$2,402	\$ (91)	(4)%	\$ 6,971	\$ 7,372	\$ (401)	(5)%
Operating expenses	1,695	1,782	(87)	(5)%	5,045	5,384	(339)	(6)%
Operating income	616	620	(4)	(1)%	1,926	1,988	(62)	(3)%
Other expense (income)—net	149	147	2	1%	463	475	(12)	(3)%
Income before income taxes	467	473	(6)	(1)%	1,463	1,513	(50)	(3)%
Income tax expense	181	180	1	1%	621	575	46	8%
Net income	<u>\$ 286</u>	<u>\$ 293</u>	<u>\$ (7)</u>	(2)%	<u>\$ 842</u>	<u>\$ 938</u>	<u>\$ (96)</u>	(10)%
Employees					26,281	28,927	(2,646)	(9)%

Operating Revenue

Operating revenue decreased primarily due to lower legacy services revenue as a result of continued access line losses and declining revenue from our traditional WAN services. In addition, operating revenue from affiliates also decreased due to reduced services provided to affiliates. These decreases in overall operating revenue were partially offset by increased revenue in our strategic services as a result of increased volume of broadband subscribers and rates on broadband services and increased volume in private line services.

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The following table summarizes our operating revenue for the three and nine months ended September 30, 2010 and 2009:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2010	2009	Increase/ (Decrease)	% Change (Dollars in millions)	2010	2009	Increase/ (Decrease)	% Change
Operating revenue:								
Strategic services	\$ 774	\$ 722	\$ 52	7%	\$2,281	\$2,164	\$ 117	5%
Legacy services	1,104	1,227	(123)	(10)%	3,385	3,809	(424)	(11)%
Affiliates and other services	433	453	(20)	(4)%	1,305	1,399	(94)	(7)%
Total operating revenue	<u>\$2,311</u>	<u>\$2,402</u>	<u>\$ (91)</u>	<u>(4)%</u>	<u>\$6,971</u>	<u>\$7,372</u>	<u>\$ (401)</u>	<u>(5)%</u>

The following table summarizes our total broadband and video subscribers and access lines by customer channel as of September 30, 2010 and 2009:

	September 30,			
	2010	2009 (in thousands)	Increase/ (Decrease)	% Change
Total broadband subscribers ⁽¹⁾	<u>2,892</u>	<u>2,743</u>	<u>149</u>	5%
Total video subscribers ⁽¹⁾	<u>963</u>	<u>888</u>	<u>75</u>	8%
Access lines ⁽¹⁾ :				
Business markets	1,913	2,036	(123)	(6)%
Mass markets	6,238	7,058	(820)	(12)%
Wholesale markets	963	1,076	(113)	(11)%
Total access lines	<u>9,114</u>	<u>10,170</u>	<u>(1,056)</u>	<u>(10)%</u>

(1) We have updated our methodology for counting our subscribers and access lines. For additional information see “Business Overview and Presentation” above.

Strategic Services

Strategic services revenue increased primarily due to an increase in the volume of broadband subscribers as well as increased rates. Strategic services revenue also increased due to increased volumes in our private line services and revenue from our increased volume of Verizon Wireless subscribers, partially offset by decreased commissions on Verizon Wireless services.

Legacy Services

Legacy services revenue decreased primarily due to a decline in local and access services revenue due to access line loss, declining demand for UNEs and reduced access services usage related to product substitution and increased competition. Legacy services also decreased due to lower revenue from our traditional WAN services, driven by industry consolidation and customer migration to more advanced technology services.

Affiliates and Other Services Revenue

Affiliates services revenue decreased primarily due to reduced telecommunication services and associated support provided as a result of a decline in customer demand for our affiliate’s legacy telecommunication service offerings driven by technological migration and competition. In addition, we had reduced support associated with

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an affiliate's winding down of its video and data products and related services. These decreases in affiliates services were partially offset by an increase in services we provided to support an affiliate's growth in its strategic service offerings. We estimate that the profit from services provided to our affiliates was approximately \$220 million and \$230 million before income taxes for the nine months ended September 30, 2010 and 2009, respectively. Other revenue, primarily USF surcharges, which we account for on a gross basis, increased primarily due to an increase in the USF contribution factor mandated by the Federal Communications Commission ("FCC"). We passed along this increase to our customers to align our USF revenue with our USF expenses.

Operating Expenses

The following table provides further detail regarding our total operating expenses for the three and nine months ended September 30, 2010 and 2009:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2010	2009	Increase/ (Decrease)	% Change	2010	2009	Increase/ (Decrease)	% Change
	(Dollars in millions)							
Cost of sales (exclusive of depreciation and amortization):								
Employee-related expenses	\$ 271	\$ 271	\$ —	— %	\$ 774	\$ 798	\$ (24)	(3)%
Other	165	164	1	1%	473	472	1	— %
Total cost of sales	436	435	1	— %	1,247	1,270	(23)	(2)%
Selling:								
Employee-related expenses	214	223	(9)	(4)%	650	741	(91)	(12)%
Marketing, advertising and external commissions	92	103	(11)	(11)%	278	316	(38)	(12)%
Other	55	63	(8)	(13)%	171	201	(30)	(15)%
Total selling	361	389	(28)	(7)%	1,099	1,258	(159)	(13)%
General, administrative and other operating:								
Employee-related expenses	145	158	(13)	(8)%	423	470	(47)	(10)%
Taxes and fees	91	103	(12)	(12)%	293	300	(7)	(2)%
Real estate and occupancy expenses	32	31	1	3%	96	102	(6)	(6)%
Other	109	124	(15)	(12)%	342	373	(31)	(8)%
Total general, administrative and other operating	377	416	(39)	(9)%	1,154	1,245	(91)	(7)%
Affiliates	51	47	4	9%	143	129	14	11%
Depreciation and amortization	470	495	(25)	(5)%	1,402	1,482	(80)	(5)%
Total operating expenses	\$1,695	\$1,782	\$ (87)	(5)%	\$5,045	\$5,384	\$ (339)	(6)%

Cost of Sales (exclusive of depreciation and amortization)

Employee-related expenses for the three months ended September 30, 2010 were flat as compared to the same period in 2009 due to lower salaries and wages related to employee reductions in our network operations,

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offset by increased severance expenses as we continue to adjust our workforce to reflect our workload. Employee-related expenses for the nine months ended September 30, 2010 decreased as compared to the same period in 2009 primarily due to lower salaries and wages related to employee reductions in our network operations as we continue to adjust our workforce to reflect our workload.

Selling Expenses

Employee-related expenses for the three months ended September 30, 2010 decreased as compared to the same period in 2009 primarily due to lower salaries, wages, commissions and benefits, partially offset by increased severance expenses driven by lower sales headcount. Employee-related expenses for the nine months ended September 30, 2010 decreased as compared to the same period in 2009 primarily due to lower salaries, wages, commissions, severance and benefits driven by lower sales headcount.

Marketing, advertising and external commissions decreased primarily due to reduced spending associated with direct mail and media. Marketing, advertising and external commissions also decreased due to improved consumer call center expenses resulting from a migration to using internal sales call centers from using third-party sales call centers.

Other expenses decreased primarily due to lower bad debt expense and professional fees.

General, Administrative and Other Operating Expenses

Employee-related expenses decreased primarily due to a decrease in pension and post-retirement benefits expenses.

QCII allocates the expense of its pension and post-retirement benefit plans to us based upon demographics of our employees compared to all the other participants. We expect to record combined pension and post-retirement benefits expenses of approximately \$125 million in 2010 as compared to \$193 million for 2009. Changes to QCII's assumptions at December 31 may increase or decrease our expected combined net periodic benefits expenses beyond 2010. The expected decrease in combined net periodic benefits expense in 2010 is primarily due to QCII's decision to no longer provide pension benefit accruals for active management employees under the qualified and non-qualified pension plans, the elimination of the qualified and non-qualified pension plan death benefits for certain retirees and reduced interest cost, partially offset by an increase in actuarial losses.

Taxes and fees decreased primarily due to lower property tax accruals, a property tax valuation settlement and lower revenue, partially offset by an increase in USF charges as a result of an increase in the USF contribution factor mandated by the FCC.

Other expenses decreased primarily due to lower professional and maintenance fees.

Affiliates Expenses

Affiliates expenses include charges for our use of long-distance services, wholesale Internet access and insurance, occupancy charges and certain retiree benefits.

Affiliates expenses increased for the nine months ended September 30, 2010 as compared to the prior year period. This increase in affiliate expenses was primarily due to insurance premium discounts and refunds recognized in 2009.

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Depreciation and Amortization

The following table provides detail regarding depreciation and amortization expense for the three and nine months ended September 30, 2010 and 2009:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2010	2009	Increase/ (Decrease)	% Change	2010	2009	Increase/ (Decrease)	% Change
(Dollars in millions)								
Depreciation and amortization:								
Depreciation	\$411	\$438	\$ (27)	(6)%	\$1,227	\$1,315	\$ (88)	(7)%
Amortization	59	57	2	4%	175	167	8	5%
Total depreciation and amortization	<u>\$470</u>	<u>\$495</u>	<u>\$ (25)</u>	(5)%	<u>\$1,402</u>	<u>\$1,482</u>	<u>\$ (80)</u>	(5)%

Lower capital expenditures and the changing mix of our investment in property, plant and equipment since 2002 have decreased our depreciation expense. If we do not significantly shorten our estimates of the useful lives of our assets, we expect that our depreciation expense will continue to decrease for the foreseeable future. Amortization expense was higher due to increases in internally developed capitalized software.

Other Consolidated Results

The following table provides detail regarding other expense (income)—net and income tax expense for the three and nine months ended September 30, 2010 and 2009:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2010	2009	Increase/ (Decrease)	% Change	2010	2009	Increase/ (Decrease)	% Change
(Dollars in millions)								
Other expense (income)—net:								
Interest expense on long-term borrowings—net	\$150	\$163	\$ (13)	(8)%	\$465	\$471	\$ (6)	(1)%
Other—net	(1)	(16)	(15)	(94)%	(2)	4	6	nm
Total other expense (income)—net	<u>\$149</u>	<u>\$147</u>	<u>\$ 2</u>	1%	<u>\$463</u>	<u>\$475</u>	<u>\$ (12)</u>	(3)%
Income tax expense	\$181	\$180	\$ 1	1%	\$621	\$575	\$ 46	8%

nm—Percentages greater than 200% and comparisons between positive and negative values or to/from zero values are considered not meaningful.

Other Expense (Income)—Net

Interest expense on long-term borrowings—net for the three months ended September 30, 2010 decreased as compared to the same period in 2009 primarily due to debt maturities. Interest expense on long-term borrowings—net for the nine months ended September 30, 2010 decreased as compared to the same period in 2009 primarily due to interest expense on our interest rate hedges partially offset by increased interest expense as a result of higher average debt levels.

Other—net includes, among other things, interest income, other interest expense (such as interest on income taxes) and gains or losses on investments. The change in other—net for the three months ended September 30, 2010 as compared to the same period in 2009 is primarily due to tax related interest from the reversal in 2009 of a prior quarter accrual for uncertain tax positions. The change in other—net for the nine months ended September 30, 2010 compared to the same period in 2009 is due to a tax-related interest expense recognized in the second quarter of 2009.

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Income Tax Expense

Income tax expense for the nine months ended September 30, 2010 increased by \$55 million as a result of the March 2010 enactments of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010. Among other things, these laws will disallow federal income tax deductions for retiree prescription drug benefits to the extent we receive reimbursements for those benefits under the Medicare Part D program. Although this tax increase does not take effect until 2013, under accounting principles generally accepted in the U.S. we recognize the full accounting impact in the period in which the laws are enacted. This increase in expense was partially offset due to the decrease in income before income taxes. The effective income tax rate is the provision for income taxes as a percentage of income before income taxes. Our effective income tax rate for each of the three months ended September 30, 2010 and 2009 was 39% and 38%, respectively. Our effective income tax rate for the nine months ended September 30, 2010 and 2009 was 42% and 38%, respectively.

Liquidity and Capital Resources

We are a wholly owned subsidiary of QSC, which is a wholly owned subsidiary of QCII. As such, factors relating to, or affecting, QCII's liquidity and capital resources could have material impacts on us, including impacts on our credit ratings, our access to capital markets and changes in the financial market's perception of us. QCII and its consolidated subsidiaries had total borrowings of \$12.979 billion and \$14.200 billion as of September 30, 2010 and December 31, 2009, respectively.

QCII has cash management arrangements between certain of its subsidiaries that include lines of credit, affiliate obligations, capital contributions and dividends. As part of these cash management arrangements, affiliates provide lines of credit to certain other affiliates. Amounts outstanding under these lines of credit and intercompany obligations vary from time to time and are classified as short-term borrowings.

Near-Term View

We expect that our cash on hand and expected net cash generated by operating activities will exceed our cash needs over the next 12 months. At September 30, 2010, we held cash and cash equivalents of \$344 million, and QCII had an additional \$1.623 billion in cash and cash equivalents as well as \$1.035 billion available under its currently undrawn revolving credit facility (referred to as the Credit Facility).

During the 12 months ended September 30, 2010, our net cash generated by operating activities totaled \$2.960 billion. For the coming 12 months, our expected financing and investing cash needs include:

- capital expenditures of approximately \$500 million or less in the remaining three months of 2010;
- capital expenditures of an as yet unknown amount in the first nine months of 2011;
- \$825 million of debt maturing in September 2011; and
- dividends to QSC.

We have significant discretion in how we use our cash to pay for capital expenditures and for other costs of our business, as only a minority of our capital expenditures is dedicated to preservation activities or government mandates. We evaluate capital expenditure projects based on expected strategic impacts (such as forecasted revenue growth or productivity, expense and service impacts) and our expected return on investment. If we are not successful in maintaining or increasing our net cash generated by operating activities in the near term, we may use this discretion to decrease our capital expenditures, which may impact future years' operating results and cash flows. Also, we lease certain facilities and equipment under various capital lease arrangements when the leasing arrangements are more favorable to us than purchasing the assets. For the nine months ended September 30, 2010, we entered into capital leases for approximately \$60 million of assets, which allowed us to reduce our initial cash outlays. We may continue to use lease financing for some portion of our capital spending.

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At September 30, 2010, our current liabilities exceeded our current assets by \$1.462 billion. This working capital deficit increased \$988 million as compared to our working capital deficit at December 31, 2009. The increase was primarily due to dividends declared to QSC, capital expenditures and the reclassification of non-current debt to current, partially offset by earnings before depreciation and amortization.

In general, we intend to refinance our debt as it matures. We expect that at any time we deem conditions favorable we will also attempt to improve our liquidity position by accessing debt markets in a manner designed to create positive economic value. The unstable economy may impair our ability to refinance maturing debt at terms that are as favorable as those from which we previously benefited or at terms that are acceptable to us.

Long-Term View

We have historically operated with a working capital deficit due to our practice of declaring and paying regular cash dividends to QSC, and it is likely that we will operate with a working capital deficit in the future. As discussed below, we continue to generate substantial cash from operations. We believe that these cash flows, combined with continued access to the capital markets to refinance debt as it comes due, will provide sufficient liquidity to continue our planned investing and financing activities.

Debt

We have a significant amount of debt maturing in the next several years, including \$825 million maturing in 2011, \$1.500 billion maturing in 2012 and \$750 million maturing in 2013. We believe that we will continue to have access to capital markets to refinance our debt as necessary. In general, we intend to refinance our debt as it matures.

The Credit Facility, which makes available to QCII \$1.035 billion of additional credit subject to certain restrictions as described below, is currently undrawn and expires in September 2013. The Credit Facility has 13 lenders, with commitments ranging from \$25 million to \$100 million. QCII's merger agreement with CenturyLink allows QCII to draw on the facility with the intent to repay the borrowings within 90 days. This facility has a cross payment default provision, and this facility and certain other debt issues of QCII and its other subsidiaries also have cross acceleration provisions. When present, these provisions could have a wider impact on liquidity than might otherwise arise from a default or acceleration of a single debt instrument. These provisions generally provide that a cross default under these debt instruments could occur if:

- QCII fails to pay any indebtedness when due in an aggregate principal amount greater than \$100 million;
- any indebtedness is accelerated in an aggregate principal amount greater than \$100 million; or
- judicial proceedings are commenced to foreclose on any of QCII's assets that secure indebtedness in an aggregate principal amount greater than \$100 million.

Upon a cross default, the creditors of a material amount of QCII's debt may elect to declare that a default has occurred under their debt instruments and to accelerate the principal amounts due to those creditors. Cross acceleration provisions are similar to cross default provisions, but permit a default in a second debt instrument to be declared only if, in addition to a default occurring under the first debt instrument, the indebtedness due under the first debt instrument is actually accelerated. As a wholly owned subsidiary of QCII, in the event of such a cross default or cross acceleration, our business operations and financial condition could be affected, potentially impacting our credit ratings and access to the capital markets.

The Credit Facility also contains various limitations, including a restriction on using any proceeds from the facility to pay settlements or judgments relating to the legal matters discussed in Note 9—Commitments and Contingencies to our condensed consolidated financial statements in Item 1 of Part I of this report. In addition, to

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the extent that QCII's earnings before interest, taxes, depreciation and amortization, or EBITDA (as defined in QCII's debt covenants), is reduced by cash settlements or judgments relating to the matters discussed in that note, QCII's debt to consolidated EBITDA ratios under certain debt agreements will be adversely affected. This could reduce QCII's liquidity and flexibility due to potential restrictions on drawing on its Credit Facility and potential restrictions on incurring additional debt under certain provisions of its debt agreements. As a wholly owned subsidiary of QCII, our business operations and financial condition could be similarly affected, potentially impacting our credit ratings and access to capital markets.

The Credit Facility will be terminated or amended at the time of the closing of QCII's merger with CenturyLink.

We may also need to obtain additional financing or investigate other methods to generate cash (such as further cost reductions or the sale of assets), but would need to do so in a manner consistent with the terms of QCII's merger agreement with CenturyLink, if:

- revenue and cash provided by operations significantly decline;
- unstable economic conditions continue to persist;
- competitive pressures increase;
- we are required to contribute a material amount of cash to QCII's pension plan; or
- QCII becomes subject to significant judgments or settlements in one or more of the matters discussed in Note 9—Commitments and Contingencies to our condensed consolidated financial statements in Item 1 of Part I of this report.

Pension Plan

Benefits paid by QCII's pension plan are paid through a trust. This pension plan is measured annually at December 31. The accounting unfunded status of the pension plan was \$790 million at December 31, 2009. Cash funding requirements can be significantly impacted by earnings on investments, the applicable discount rate used to value the benefit obligation, changes in the plan and funding laws and regulations. As a result, it is difficult to determine future funding requirements with a high level of precision; however, in general, current funding laws and regulations require funding deficits to be paid over a seven year period unless the plan is fully funded before then. QCII will not be required to make a cash contribution to this plan in 2010 and based on current funding laws and regulations QCII will not be required to make a contribution in 2011. It is very likely, based on current funding laws and regulations, that significant contributions will be required in 2012 and beyond. The amount of any required contributions in 2012 and beyond will depend on earnings on investments, discount rates, changes in the plan and funding laws and regulations.

Historically, QCII has only required us to pay our portion of its pension contribution. Our contributions are not segregated or restricted to pay amounts due to our employees and may be used to provide benefits to other employees of QCII's affiliates.

Post-Retirement Benefits

Certain of QCII's post-retirement health care and life insurance benefits plans are unfunded. As of December 31, 2009, the unfunded status of all of QCII's post-retirement benefit plans was \$2.525 billion. A trust holds assets that are used to help cover the health care costs of retirees who are former occupational (also referred to as union) employees.

As of December 31, 2009, the fair value of the trust assets was \$863 million; however, a portion of these assets is comprised of investments with restricted liquidity. QCII believes that, as of December 31, 2009, the more liquid assets in the trust would be adequate to provide continuing reimbursements for its occupational

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post-retirement health care costs for approximately five years. Thereafter, covered benefits for its eligible retirees who are former occupational employees will be paid either directly by us or from the trust as the remaining assets become liquid. This five year period could be substantially shorter or longer depending on returns on plan assets, the timing of maturities of illiquid plan assets and future changes in benefits. QCII's estimate of the annual long-term rate of return on the plan assets is 8.0% based on the currently held assets; however, actual returns could vary widely in any given year.

Our eligible employees participate in the QCII post-retirement plan. The amounts contributed by us through QCII are not segregated or restricted to pay amounts due to our employees and may be used to provide benefits to other employees of QCII's affiliates. Historically, QCII has only required us to pay our portion of its post-retirement contribution.

Historical View

The following table summarizes cash flow activities for the nine months ended September 30, 2010 and 2009:

	Nine Months Ended September 30,			
	2010	2009	Increase/ (Decrease)	% Change
	(Dollars in millions)			
Cash flows:				
Provided by operating activities	\$2,236	\$2,443	\$ (207)	(8)%
Used for investing activities	889	828	61	7%
Used for financing activities	2,017	778	1,239	159%

nm—Percentages greater than 200% and comparisons between positive and negative values or to/from zero values are considered not meaningful.

Operating Activities

Cash provided by operating activities decreased primarily due to the decline in cash received from customers as a result of decreased revenue. Cash provided by operating activities also decreased due to additional cash paid for interest caused by higher average debt levels.

Investing Activities

Cash used for investing activities increased primarily due to increased capital expenditures, partially offset by cash provided by interest in net proceeds from investments managed by QSC. The increase in capital spending was due to a cautious investment climate in late 2008 and early 2009, increased spending on our strategic initiatives and timing of cash payments.

Financing Activities

For the nine months ended September 30, 2010, we repaid \$519 million of long-term borrowings including current maturities and we paid \$1.500 billion in dividends to QSC. We may continue to declare and pay dividends to QSC in excess of our earnings to the extent permitted by applicable law. Our debt covenants do not limit the amount of dividends we can pay to QSC. We were in compliance with all provisions and covenants of our borrowings as of September 30, 2010.

Letters of Credit

We maintain letter of credit arrangements with various financial institutions for up to \$57 million. We had outstanding letters of credit of approximately \$51 million as of September 30, 2010.

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Credit Ratings

Since QCII's announcement of its pending merger with CenturyLink:

- on August 13, 2010, Moody's Investors Service upgraded our rating from Ba1 to Baa3 (investment grade);
- Standard & Poor's placed our rating on "CreditWatch" with developing implications, meaning that S&P could raise or lower the rating; and
- Fitch Ratings affirmed its previous rating of BBB- with a stable outlook.

Risk Management

We are exposed to market risks arising from changes in interest rates. The objective of our interest rate risk management program is to manage the level and volatility of our interest expense. We have used derivative financial instruments to manage our interest rate risk exposure on our debt and we may continue to employ them in the future.

There were no material changes to market risks arising from changes in interest rates for the nine months ended September 30, 2010, when compared to the disclosures provided in our Annual Report on Form 10-K for the year ended December 31, 2009.

Off-Balance Sheet Arrangements

We have no special purpose or limited purpose entities that provide off-balance sheet financing, liquidity, or market or credit risk support, and we do not engage in leasing, hedging, research and development services, or other relationships that expose us to any significant liabilities that are not reflected on the face of the condensed consolidated financial statements. There were no substantial changes to our off-balance sheet arrangements or contractual commitments in the nine months ended September 30, 2010, when compared to the disclosures provided in our Annual Report on Form 10-K for the year ended December 31, 2009.

Website Access and Important Investor Information

Our website address is www.qwest.com, and we routinely post important investor information in the "Investor Relations" section of our website at investor.qwest.com. The information contained on, or that may be accessed through, our website is not part of this report.

Special Note Regarding Forward-Looking Statements

This Form 10-Q contains or incorporates by reference forward-looking statements about our financial condition, operating results and business. These statements include, among others:

- statements concerning the benefits that we expect will result from our business activities and certain transactions we have completed, such as increased revenue, decreased expenses and avoided expenses and capital or other expenditures; and
- statements of our expectations, beliefs, future plans and strategies, anticipated developments and other matters that are not historical facts.

These statements may be made expressly in this document or may be incorporated by reference to other documents we have filed or will file with the Securities and Exchange Commission, or SEC. You can find many of these statements by looking for words such as "may," "would," "could," "should," "plan," "believes," "expects," "anticipates," "estimates," or similar expressions used in this document or in documents incorporated by reference in this document.

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These forward-looking statements are subject to numerous assumptions, risks and uncertainties that may cause our actual results to be materially different from any future results expressed or implied by us in those statements. Some of these risks are described in Item 1A of Part II of this report.

These risk factors should be considered in connection with any written or oral forward-looking statements that we or persons acting on our behalf may issue. Given these uncertainties, we caution investors not to unduly rely on our forward-looking statements. We do not undertake any obligation to review or confirm analysts' expectations or estimates or to release publicly any revisions to any forward-looking statements to reflect events or circumstances after the date of this document or to reflect the occurrence of unanticipated events. Further, the information about our intentions contained in this document is a statement of our intentions as of the date of this document and is based upon, among other things, the existing regulatory environment, industry conditions, market conditions and prices, the economy in general and our assumptions as of such date. We may change our intentions, at any time and without notice, based upon any changes in such factors, in our assumptions or otherwise.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information under the heading "Risk Management" in Item 2 of Part I of this report is incorporated herein by reference.

ITEM 4. CONTROLS AND PROCEDURES

The effectiveness of our or any system of disclosure controls and procedures is subject to certain limitations, including the exercise of judgment in designing, implementing and evaluating the controls and procedures, the assumptions used in identifying the likelihood of future events and the inability to eliminate misconduct completely. As a result, there can be no assurance that our disclosure controls and procedures will detect all errors or fraud. By their nature, our or any system of disclosure controls and procedures can provide only reasonable assurance regarding management's control objectives.

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we evaluated the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, or the "Exchange Act") as of September 30, 2010. On the basis of this review, our management, including our Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures are designed, and are effective, to give reasonable assurance that the information required to be disclosed by us in reports that we file under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and to ensure that information required to be disclosed in the reports filed or submitted under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, in a manner that allows timely decisions regarding required disclosure.

There were no changes in our internal control over financial reporting that occurred in the third quarter of 2010 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II—OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information contained in Note 9—Commitments and Contingencies to our condensed consolidated financial statements in Item 1 of Part I of this report is incorporated herein by reference.

ITEM 1A. RISK FACTORS

Risks Relating to QCII's Pending Merger with CenturyLink

QCII's merger with CenturyLink is subject to closing conditions, including government approvals, which could result in additional conditions that adversely affect QCII or which could cause the merger to be delayed or abandoned.

The completion of the CenturyLink merger is subject to certain closing conditions, including the absence of injunctions or other legal restrictions and the absence of a material adverse effect on either company. In addition, the merger remains subject to approvals from the Federal Communications Commission, or FCC, and several state public service or public utility commissions or other similar state regulators. These regulatory entities could impose requirements or obligations as conditions for their approvals. Despite QCII's best efforts, QCII may not be able to satisfy the various closing conditions and obtain the necessary approvals. In addition, any required conditions to these approvals could adversely affect the combined company or could result in the delay or abandonment of the merger.

Failure to complete the CenturyLink merger could negatively impact QCII and us.

If the CenturyLink merger is not completed, QCII would still remain liable for significant transaction costs and the focus of QCII's management would have been diverted from seeking other potential strategic opportunities, in each case without realizing any benefits of a completed merger. Depending on the reasons for not completing the merger, QCII could also be required to pay CenturyLink a termination fee of \$350 million. For these and other reasons, a failed merger could adversely affect QCII's business, operating results or financial condition, which in turn could adversely affect our business or financial condition. In addition, the trading price of QCII's and our securities could be adversely affected to the extent that the current price reflects an assumption that the merger will be completed.

While the CenturyLink merger is pending, QCII and we are subject to business uncertainties and contractual restrictions that could adversely affect our business.

Our employees, customers and suppliers may have uncertainties about the effects of the merger. Although QCII and we intend to take actions designed to reduce any adverse effects of these uncertainties, they may impair our ability to attract, retain and motivate key employees and could cause customers, suppliers and others that deal with us to try to change our existing business relationships.

Employee retention and recruitment while the merger is pending could be difficult, as employees and prospective employees could be uncertain about their future roles with a combined company. In addition, the pursuit of the merger and preparations for integration will place a significant burden on many employees and internal resources. If, despite QCII's and our efforts, key employees depart or fail to accept employment with us because of these uncertainties and changes, or because they do not wish to remain with a combined company, our business and operating results could be adversely affected.

While the merger is pending, some of our customers could delay or forgo purchasing decisions and suppliers could seek additional rights or benefits from us. In addition, the merger agreement restricts QCII and us from taking certain actions with respect to our business and financial affairs without CenturyLink's consent, and these restrictions could be in place for an extended period of time if the merger is delayed. For these and other reasons, the pendency of the merger could adversely affect our business, operating results or financial condition.

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If completed, QCII's merger with CenturyLink may not achieve the intended results.

The merger will involve the combination of two companies that currently operate as independent public companies. The combined company will need to devote management attention and resources to integrate QCII's and CenturyLink's businesses. In addition, the combined company may face difficulties with the integration process. For example:

- the combined company may not realize the anticipated cost savings and operating synergies at expected levels or in the expected timeframe;
- existing customers and suppliers may decide not to do business with the combined company;
- the costs of integrating QCII's policies, procedures, operations, technologies and systems with those of CenturyLink could be higher than expected;
- the integration process could consume significant time and attention on the part of the combined company's management, thereby diverting attention from day-to-day operations; or
- the combined company may not be able to integrate employees from the two companies while maintaining existing levels of sales and customer service.

For these and other reasons, the merger may not achieve the intended results.

Risks Affecting Our Business

Increasing competition, including product substitution, continues to cause access line losses, which has adversely affected and could continue to adversely affect our operating results and financial condition.

We compete in a rapidly evolving and highly competitive market, and we expect competition to continue to intensify. We are facing greater competition from cable companies, wireless providers, resellers and sales agents (including ourselves) and facilities-based providers using their own networks as well as those leasing parts of our network. In addition, regulatory developments over the past several years have generally increased competitive pressures on our business. Due to some of these and other factors, we continue to lose access lines.

We are continually evaluating our responses to these competitive pressures. Some of our more recent responses are expanded broadband capabilities and strategic partnerships. We also remain focused on customer service and providing customers with simple and integrated solutions, including, among other things, product bundles and packages. However, we may not be successful in these efforts. We may not be able to distinguish our offerings and service levels from those of our competitors, and we may not be successful in integrating our product offerings, especially products for which we act as a reseller or sales agent such as wireless and video services. If these initiatives are unsuccessful or insufficient, we are otherwise unable to sufficiently stem or offset our continuing access line losses and our revenue declines significantly without corresponding cost reductions, this would adversely affect our operating results and financial condition, as well as our ability to service debt and pay other obligations.

Unfavorable general economic conditions in the United States could negatively impact our operating results and financial condition.

Unfavorable general economic conditions, including the unstable economy and the current credit market environment, could negatively affect our business. While it is often difficult for us to predict the impact of general economic conditions on our business, these conditions could adversely affect the affordability of and consumer demand for some of our products and services and could cause customers to shift to lower priced products and services or to delay or forgo purchases of our products and services. One or more of these circumstances could cause our revenue to decline. Also, our customers may not be able to obtain adequate access to credit, which could affect their ability to make timely payments to us. If that were to occur, we could be required to increase our allowance for doubtful accounts, and the number of days outstanding for our accounts receivable could increase. In addition, as discussed below under the heading "Risks Affecting our Liquidity," due

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to the unstable economy and the current credit market environment, we may not be able to refinance maturing debt at terms that are as favorable as those from which we previously benefited, at terms that are acceptable to us or at all. For these reasons, among others, if the current economic conditions persist or decline, this could adversely affect our operating results and financial condition, as well as our ability to service debt and pay other obligations.

Consolidation among other participants in the telecommunications industry may allow our competitors to compete more effectively against us, which could adversely affect our operating results and financial condition.

The telecommunications industry has experienced some consolidation, and several of our competitors have consolidated with other telecommunications providers. This consolidation results in competitors that are larger and better financed and affords our competitors increased resources and greater geographical reach, thereby enabling those competitors to compete more effectively against us. We have experienced and expect further increased pressures as a result of this consolidation and in turn have been and may continue to be forced to respond with lower profit margin product offerings and pricing plans in an effort to retain and attract customers. These pressures could adversely affect our operating results and financial condition, as well as our ability to service debt and pay other obligations.

Rapid changes in technology and markets could require substantial expenditure of financial and other resources in excess of contemplated levels, and any inability to respond to those changes could reduce our market share and adversely affect our operating results and financial condition.

The telecommunications industry is experiencing significant technological changes, and our ability to execute our business plans and compete depends upon our and our affiliates' ability to develop and deploy new products and services. The development and deployment of new products and services could also require substantial expenditure of financial and other resources in excess of contemplated levels. If we are not able to develop new products and services to keep pace with technological advances, or if those products and services are not widely accepted by customers, our ability to compete could be adversely affected and our market share could decline. Any inability to keep up with changes in technology and markets could also adversely affect our operating results and financial condition, as well as our ability to service debt and pay other obligations.

Our reseller and sales agency arrangements expose us to a number of risks, one or more of which may adversely affect our business and operating results.

We rely on reseller and sales agency arrangements with other companies to provide some of the services that we sell to our customers, including video services and wireless products and services. If we fail to extend or renegotiate these arrangements as they expire from time to time or if these other companies fail to fulfill their contractual obligations to us or our customers, we may have difficulty finding alternative arrangements and our customers may experience disruptions to their services. In addition, as a reseller or sales agent, we do not control the availability, retail price, design, function, quality, reliability, customer service or branding of these products and services, nor do we directly control all of the marketing and promotion of these products and services. To the extent that these other companies make decisions that negatively impact our ability to market and sell their products and services, our business plans and goals and our reputation could be negatively impacted. If these reseller and sales agency arrangements are unsuccessful due to one or more of these risks, our business and operating results may be adversely affected.

Third parties may claim we infringe upon their intellectual property rights, and defending against these claims could adversely affect our profit margins and our ability to conduct business.

From time to time, we receive notices from third parties or are named in lawsuits filed by third parties claiming we have infringed or are infringing upon their intellectual property rights. We may receive similar notices or be involved in similar lawsuits in the future. Responding to these claims may require us to expend

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significant time and money defending our use of affected technology, may require us to enter into licensing agreements requiring royalty payments that we would not otherwise have to pay or may require us to pay damages. If we are required to take one or more of these actions, our profit margins may decline. In addition, in responding to these claims, we may be required to stop selling or redesign one or more of our products or services, which could significantly and adversely affect the way we conduct business.

Risks Relating to Legal and Regulatory Matters

Any adverse outcome of the KPNQwest litigation could have a material adverse impact on our financial condition and operating results, on the trading price of our debt securities and on our ability to access the capital markets.

As described in Note 9—Commitments and Contingencies to our condensed consolidated financial statements in Item 1 of Part I of this report, the KPNQwest matters present material and significant risks to QCII and us. In the aggregate, the plaintiffs in the KPNQwest matters have sought billions of dollars in damages. In addition, the outcome of one or more of these matters could have a negative impact on the outcomes of the other matters. QCII continues to defend against these matters vigorously and is currently unable to provide any estimate as to the timing of their resolution.

We can give no assurance as to the impacts on QCII's and our financial results or financial condition that may ultimately result from these matters. The ultimate outcomes of these matters are still uncertain, and substantial settlements or judgments in these matters could have a significant impact on QCII and us. The magnitude of such settlements or judgments resulting from these matters could materially and adversely affect QCII's financial condition and ability to meet its debt obligations, potentially impacting its credit ratings, its ability to access capital markets and its compliance with debt covenants. In addition, the magnitude of any such settlements or judgments may cause QCII to draw down significantly on its cash balances, which might force it to obtain additional financing or explore other methods to generate cash. Such methods could include issuing additional securities or selling assets. As a wholly owned subsidiary of QCII, our business operations and financial condition could be similarly affected.

Further, there are other material proceedings pending against QCII as described in Note 9—Commitments and Contingencies to our condensed consolidated financial statements in Item 1 of Part I of this report that, depending on their outcome, may have a material adverse effect on QCII's and our financial position. Thus, we can give no assurances as to the impacts on QCII's and our operating results or financial condition as a result of these matters.

We operate in a highly regulated industry and are therefore exposed to restrictions on our manner of doing business and a variety of claims relating to such regulation.

We are subject to significant regulation by the FCC, which regulates interstate communications, and state utility commissions, which regulate intrastate communications. Generally, we must obtain and maintain certificates of authority from the FCC and regulatory bodies in most states where we offer regulated services, and we are subject to numerous, and often quite detailed, requirements under federal, state and local laws, rules and regulations. Accordingly, we cannot ensure that we are always in compliance with all these requirements at any single point in time. The agencies responsible for the enforcement of these laws, rules and regulations may initiate inquiries or actions based on customer complaints or on their own initiative.

Regulation of the telecommunications industry is changing rapidly, and the regulatory environment varies substantially from state to state. The state legislatures and state utility commissions in our local service area have adopted reduced or modified forms of regulation for retail services. These changes also generally allow more flexibility for rate changes and for new product introduction, and they enhance our ability to respond to competition. Despite these regulatory changes, a substantial portion of our local voice services revenue remains subject to FCC and state utility commission pricing regulation, which could expose us to unanticipated price declines. For instance, in 2010 the state utility commission in Arizona may consider a price cap plan that will

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govern the rates that we charge in that state. The FCC is also considering changing the rates that carriers can charge each other for originating, carrying and terminating traffic and for local access facilities. Also under review by the FCC and state commissions are the intercarrier compensation issues arising from the delivery of traffic destined for entities that offer conference and chat line services for free (known in the industry as “access stimulation,” or “traffic pumping”), and of traffic bound for Internet service providers that cross local exchange boundaries (known as “VNXX traffic”). The FCC and state commissions are also considering changes to funds they have established to subsidize service to high-cost areas. Changes to how those funds are distributed could result in us receiving less in universal service funding, and changes to how the funds are collected could make some of our services less competitive. There can be no assurance that future regulatory, judicial or legislative activities will not have a material adverse effect on our operations, or that regulators or third parties will not raise material issues with regard to our compliance or noncompliance with applicable regulations.

All of our operations are also subject to a variety of environmental, safety, health and other governmental regulations. We monitor our compliance with federal, state and local regulations governing the management, discharge and disposal of hazardous and environmentally sensitive materials. Although we believe that we are in compliance with these regulations, our management, discharge or disposal of hazardous and environmentally sensitive materials might expose us to claims or actions that could have a material adverse effect on our business, financial condition and operating results.

Risks Affecting Our Liquidity

QCII’s high debt levels pose risks to our viability and may make us more vulnerable to adverse economic and competitive conditions, as well as other adverse developments.

Our ultimate parent, QCII, continues to carry significant debt. As of September 30, 2010, our consolidated debt was approximately \$8.0 billion, which was included in QCII’s consolidated debt of approximately \$13.0 billion as of that date. Approximately \$4.4 billion of QCII’s debt, which includes approximately \$3.1 billion of our debt obligations, comes due over the next three years. The \$4.4 billion amount also includes \$1.118 billion of QCII’s 3.50% Convertible Senior Notes due 2025 (referred to as the 3.50% Convertible Senior Notes), which QCII expects to repurchase or redeem in the fourth quarter of 2010. While we currently believe QCII and we will have the financial resources to meet our obligations when they come due, we cannot fully anticipate our future condition or that of QCII, the credit markets or the economy generally. We may have unexpected costs and liabilities, and we may have limited access to financing. In addition, it is the current expectation of QCII’s Board of Directors that QCII will continue to pay a quarterly cash dividend. Cash used by QCII to pay dividends will not be available for other purposes, including the repayment of debt.

We may periodically need to obtain financing in order to meet our debt obligations as they come due. Due to the unstable economy and the current credit market environment, we may not be able to refinance maturing debt at terms that are as favorable as those from which we previously benefited, at terms that are acceptable to us or at all. We may also need to obtain additional financing or investigate other methods to generate cash (such as further cost reductions or the sale of assets), but would need to do so in a manner consistent with the terms of QCII’s merger agreement with CenturyLink, if revenue and cash provided by operations decline, if economic conditions weaken, if competitive pressures increase, if QCII or we are required to contribute a material amount of cash to QCII’s pension plan, if QCII or we are required to begin to pay other post-retirement benefits significantly earlier than is anticipated, or if QCII becomes subject to significant judgments or settlements in one or more of the matters discussed in Note 9—Commitments and Contingencies to our condensed consolidated financial statements in Item 1 of Part I of this report. We can give no assurance that this additional financing will be available on terms that are acceptable to us or at all. Also, we may be impacted by factors relating to or affecting our liquidity and capital resources due to perception in the market, impacts on our credit ratings or provisions in our financing agreements that may restrict our flexibility under certain conditions.

QCII’s \$1.035 billion revolving Credit Facility, which is currently undrawn, has a cross payment default provision, and the Credit Facility and certain other debt issues of QCII and its other subsidiaries have cross acceleration provisions. When present, these provisions could have a wider impact on liquidity than might

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otherwise arise from a default or acceleration of a single debt instrument. As a subsidiary of QCII, any such event could adversely affect our ability to conduct business or access the capital markets and could adversely impact our credit ratings. In addition, the Credit Facility contains various limitations, including a restriction on using any proceeds from the facility to pay settlements or judgments relating to the legal matters discussed in Note 9—Commitments and Contingencies to our condensed consolidated financial statements in Item 1 of Part I of this report.

The degree to which we, together with QCII, are leveraged may have other important limiting consequences, including the following:

- placing us at a competitive disadvantage as compared with our less leveraged competitors;
- making us more vulnerable to downturns in general economic conditions or in any of our businesses;
- limiting our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate; and
- impairing our ability to obtain additional financing in the future for working capital, capital expenditures or general corporate purposes.

We may be unable to significantly reduce the substantial capital requirements or operating expenses necessary to continue to operate our business, which may in turn affect our operating results.

The industry in which we operate is capital intensive, and we anticipate that our capital requirements will continue to be significant in the coming years. Although we have reduced our operating expenses over the past few years, we may be unable to further significantly reduce these costs, even if revenue in some areas of our business is decreasing. While we believe that our planned level of capital expenditures will meet both our maintenance and our core growth requirements going forward, this may not be the case if circumstances underlying our expectations change.

Adverse changes in the value of assets or obligations associated with QCII's employee benefit plans could negatively impact QCII's liquidity, which may in turn affect our business and liquidity.

Our employees participate in employee benefit plans sponsored by QCII.

QCII maintains a qualified pension plan, a non-qualified pension plan and post-retirement benefit plans. The funded status of these plans is the difference between the value of all plan assets and benefit obligations. The accounting unfunded status of QCII's pension plan was \$790 million at December 31, 2009. The process of calculating benefit obligations is complex. Adverse changes in interest rates or market conditions, among other assumptions and factors, could cause a significant increase in QCII's benefit obligations or a significant decrease in the value of plan assets. With respect to QCII's qualified pension plan, adverse changes could require QCII to contribute a material amount of cash to the plan or could accelerate the timing of any required cash payments. The amounts contributed by us through QCII are not segregated or restricted and may be used to provide benefits to employees of QCII's other subsidiaries. QCII determines our cash contribution and, historically, has only required us to pay our portion of its required pension contribution. QCII will not be required to make a cash contribution to this plan in 2010 and based on current funding laws and regulations QCII will not be required to make a contribution in 2011. It is very likely, based on current funding laws and regulations, that significant contributions will be required in 2012 and beyond. The amount of any required contributions in 2012 and beyond will depend on earnings on investments, discount rates, changes in the plan and funding laws and regulations. Any future material cash contributions in 2011 and beyond could have a negative impact on QCII's liquidity by reducing its cash flows, which in turn could affect our liquidity.

Because we are a wholly owned subsidiary of QCII, these events could adversely affect our liquidity or our ability to conduct our business or access the capital markets.

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The cash needs of our affiliated companies consume a significant amount of the cash we generate.

We regularly declare and pay dividends to our direct parent, QSC. We may declare and pay dividends in excess of our earnings to the extent permitted by applicable law, which may consume a significant amount of the cash we generate. Our debt covenants do not limit the amount of dividends we can pay to our parent.

Our debt agreements and the debt agreements of QCII allow us and QCII to incur significantly more debt, which could exacerbate the other risks described in this report.

The terms of QCII's and our debt instruments permit both QCII and us to incur additional indebtedness. Additional debt may be necessary for many reasons, including to adequately respond to competition, to comply with regulatory requirements related to our service obligations or for financial reasons alone. Incremental borrowings or borrowings at maturity on terms that impose additional financial risks to our various efforts to improve our operating results and financial condition could exacerbate the other risks described in this report.

Other Risks Relating to Qwest

If conditions or assumptions differ from the judgments, assumptions or estimates used in our critical accounting policies, the accuracy of our financial statements and related disclosures could be affected.

The preparation of financial statements and related disclosures in conformity with U.S. generally accepted accounting principles requires management to make judgments, assumptions and estimates that affect the amounts reported in our consolidated financial statements and accompanying notes. Our critical accounting policies, which are described in our Annual Report on Form 10-K for the year ended December 31, 2009, describe those significant accounting policies and methods used in the preparation of our consolidated financial statements that are considered "critical" because they require judgments, assumptions and estimates that materially impact our consolidated financial statements and related disclosures. As a result, if future events or assumptions differ significantly from the judgments, assumptions and estimates in our critical accounting policies, these events or assumptions could have a material impact on our consolidated financial statements and related disclosures.

Taxing authorities may determine we owe additional taxes relating to various matters, which could adversely affect our financial results.

We are included in the consolidated federal income tax return of QCII. As such, we could be severally liable for tax examinations and adjustments attributed to other members of the QCII affiliated group. As a significant taxpayer, QCII is subject to frequent and regular audits by the Internal Revenue Service as well as state and local tax authorities. These audits could subject us to tax liabilities if adverse positions are taken by these tax authorities.

Tax sharing agreements have been executed between QCII and previous affiliates, and QCII believes the liabilities, if any, arising from adjustments to previously filed returns would be borne by the affiliated group member determined to have a deficiency under the terms and conditions of such agreements and applicable tax law. We have not generally provided for liabilities attributable to current or former affiliated companies or for claims they have asserted or may assert against us.

We believe that we have adequately provided for tax contingencies. However, QCII's tax audits and examinations may result in tax liabilities that differ materially from those that we have recorded in our condensed consolidated financial statements. Because the ultimate outcomes of all of these matters are uncertain, we can give no assurance as to whether an adverse result from one or more of them will have a material effect on our financial results.

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If we fail to extend or renegotiate our collective bargaining agreements with our labor unions as they expire from time to time, or if our unionized employees were to engage in a strike or other work stoppage, our business and operating results could be materially harmed.

We are a party to collective bargaining agreements with our labor unions, which represent a significant number of our employees. Our current four-year agreements with the Communications Workers of America and the International Brotherhood of Electrical Workers expire on October 6, 2012. Although we believe that our relations with our employees and unions are satisfactory, no assurance can be given that we will be able to successfully extend or renegotiate our collective bargaining agreements as they expire from time to time. The impact of future negotiations, including changes in wages and benefit levels, could have a material impact on our financial results. Also, if we fail to extend or renegotiate our collective bargaining agreements, if significant disputes with our unions arise, or if our unionized workers engage in a strike or other work stoppage, we could incur higher ongoing labor costs or experience a significant disruption of operations, which could have a material adverse effect on our business.

ITEM 6. EXHIBITS

Exhibits identified in parentheses below are on file with the SEC and are incorporated herein by reference. All other exhibits are provided as part of this electronic submission.

<u>Exhibit Number</u>	<u>Description</u>
(3.1)	Restated Articles of Incorporation of Qwest Corporation (incorporated by reference to Qwest Corporation's Annual Report on Form 10-K for the year ended December 31, 1997, File No. 001-03040).
(3.2)	Articles of Amendment to the Articles of Incorporation of Qwest Corporation (incorporated by reference to Qwest Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 2000, File No. 001-03040).
(3.3)	Amended and Restated Bylaws of Qwest Corporation (incorporated by reference to Qwest Corporation's Annual Report on Form 10-K for the year ended December 31, 2002, File No. 001-03040).
(4.1)	Indenture, dated as of April 15, 1990, by and between Mountain States Telephone and Telegraph Company and The First National Bank of Chicago (incorporated by reference to Qwest Corporation's Annual Report on Form 10-K for the year ended December 31, 2002, File No. 001-03040).
(4.2)	First Supplemental Indenture, dated as of April 16, 1991, by and between U S WEST Communications, Inc. and The First National Bank of Chicago (incorporated by reference to Qwest Corporation's Annual Report on Form 10-K for the year ended December 31, 2002, File No. 001-03040).
(4.3)	Indenture, dated as of October 15, 1999, by and between U S West Communications, Inc. and Bank One Trust Company, N.A. (incorporated by reference to Qwest Corporation's Annual Report on Form 10-K for the year ended December 31, 1999, File No. 001-03040).
(4.4)	Officer's Certificate of Qwest Corporation, dated as of March 12, 2002 (including forms of 8 ⁷ / ₈ % notes due March 15, 2012) (incorporated by reference to Qwest Corporation's Form S-4, File No. 333-115119).
(4.5)	First Supplemental Indenture, dated as of August 19, 2004, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Qwest Communications International Inc.'s Quarterly Report on Form 10-Q for the quarter ended September 30, 2004, File No. 001-15577).

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<u>Exhibit Number</u>	<u>Description</u>
(4.6)	Second Supplemental Indenture, dated as of November 23, 2004, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Qwest Corporation's Current Report on Form 8-K filed November 23, 2004, File No. 001-03040).
(4.7)	Third Supplemental Indenture, dated as of June 17, 2005, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Qwest Corporation's Current Report on Form 8-K filed June 23, 2005, File No. 001-03040).
(4.8)	Fourth Supplemental Indenture, dated August 8, 2006, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Qwest Corporation's Current Report on Form 8-K filed August 8, 2006, File No. 001-03040).
(4.9)	Fifth Supplemental Indenture, dated May 16, 2007, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Qwest Corporation's Current Report on Form 8-K filed May 18, 2007, File No. 001-03040).
(4.10)	Sixth Supplemental Indenture, dated April 13, 2009, by and between Qwest Corporation and U.S. Bank National Association (incorporated by reference to Qwest Corporation's Current Report on Form 8-K filed April 13, 2009, File No. 001-03040).
(10.1)	Registration Rights Agreement, dated April 13, 2009, among Qwest Corporation and the initial purchasers listed therein (incorporated by reference to Qwest Corporation's Current Report on Form 8-K filed April 13, 2009, File No. 001-03040).
(10.2)	Aircraft Time Sharing Agreement, dated December 1, 2008, by and between Qwest Corporation and Edward A. Mueller (incorporated by reference to Qwest Communications International Inc.'s Annual Report on Form 10-K for the year ended December 31, 2008, File No. 001-15577).
(10.3)	First Amendment to Aircraft Time Sharing Agreement, dated July 29, 2010, by and between Qwest Corporation and Edward A. Mueller (incorporated by reference to Qwest Communications International Inc.'s Quarterly Report on Form 10-Q for the quarter ended June 30, 2010, File No. 001-15577).
12	Calculation of Ratio of Earnings to Fixed Charges.
31.1	Chief Executive Officer Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Chief Financial Officer Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
()	Previously filed.

In accordance with Item 601(b) (4) (iii) (A) of Regulation S-K, copies of certain instruments defining the rights of holders of certain of our long-term debt are not filed herewith. Pursuant to this regulation, we hereby agree to furnish a copy of any such instrument to the SEC upon request.

SIGNATURE

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

QWEST CORPORATION

By: / s / R. W ILLIAM J OHNSTON
R. William Johnston
Senior Vice President, Controller and
Chief Accounting Officer
(Chief Accounting Officer and
Duly Authorized Officer)

November 3, 2010

QWEST CORPORATION
CALCULATION OF RATIO OF EARNINGS TO FIXED CHARGES ⁽²⁾
(UNAUDITED)

	Nine Months Ended September 30, 2010	Years Ended December 31,				
		2009	2008	2007	2006	2005
Income before income taxes and cumulative effect of changes in accounting principles	\$ 1,463	\$1,921	\$2,267	\$2,440	\$1,882	\$1,628
Add: estimated fixed charges	519	705	671	682	700	700
Add: estimated amortization of capitalized interest	8	11	12	10	10	12
Less: interest capitalized	(8)	(10)	(14)	(12)	(12)	(10)
Total earnings available for fixed charges	<u>\$ 1,982</u>	<u>\$2,627</u>	<u>\$2,936</u>	<u>\$3,120</u>	<u>\$2,580</u>	<u>\$2,330</u>
Estimate of interest factor on rentals	\$ 46	\$ 63	\$ 68	\$ 62	\$ 72	\$ 82
Interest expense, including amortization of premiums, discounts and debt issuance costs ⁽¹⁾	465	632	589	608	616	608
Interest capitalized	8	10	14	12	12	10
Total fixed charges	<u>\$ 519</u>	<u>\$ 705</u>	<u>\$ 671</u>	<u>\$ 682</u>	<u>\$ 700</u>	<u>\$ 700</u>
Ratio of earnings to fixed charges	3.8	3.7	4.4	4.6	3.7	3.3

(1) Interest expense includes only interest related to long-term borrowings and capital lease obligations.

(2) We have reclassified certain prior year amounts to conform to the current quarter presentation.

CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Edward A. Mueller, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Qwest Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 3, 2010

/s/ E DWARD A. M UELLER

Edward A. Mueller
Chief Executive Officer

CERTIFICATION OF CHIEF FINANCIAL OFFICER

I, Joseph J. Euteneuer, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Qwest Corporation;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 3, 2010

/s/ J OSEPH J. E UTENEUER

Joseph J. Euteneuer

Executive Vice President and Chief Financial Officer

CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER CERTIFICATION

Each of the undersigned hereby certifies, for the purposes of section 1350 of chapter 63 of title 18 of the United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, in his capacity as an officer of Qwest Corporation ("Qwest"), that, to his knowledge, the Quarterly Report of Qwest on Form 10-Q for the quarter ended September 30, 2010, fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934 and that the information contained in such report fairly presents, in all material respects, the financial condition and results of operations of Qwest. This written statement is being furnished to the Securities and Exchange Commission as an exhibit to such Form 10-Q. A signed original of this statement has been provided to Qwest and will be retained by Qwest and furnished to the Securities and Exchange Commission or its staff upon request.

Dated: November 3, 2010

By: /s/ E DWARD A. M UELLER
Edward A. Mueller
Chief Executive Officer

Dated: November 3, 2010

By: /s/ J OSEPH J. E UTENEUER
Joseph J. Euteneuer
Executive Vice President and Chief Financial Officer