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

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**FORM 10-Q**

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

For the quarterly period ended June 30, 2009

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)

**84-0273800**

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

**1801 California Street, Denver, Colorado**

(Address of principal executive offices)

**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 July 28, 2009, one share of Qwest Corporation common stock was outstanding.

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**QWEST CORPORATION**

**FORM 10-Q**

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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 include lines used to provide services to our external customers, as well as lines used by us and our affiliates.
- *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 that operate 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.
- *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 governmental and business customers.
- *Dedicated Internet Access (DIA).* Internet access ranging from 128 kilobits per second to 10 gigabits per second.
- *Facility Costs.* Third-party telecommunications expenses we incur for using other carriers' networks to provide services to our customers.
- *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.
- *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 ATM and frame relay 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		Six Months Ended	
	June 30,		June 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Operating revenue:				
Operating revenue	\$2,035	\$2,151	\$4,112	\$4,328
Operating revenue—affiliates	428	456	858	903
Total operating revenue	<u>2,463</u>	<u>2,607</u>	<u>4,970</u>	<u>5,231</u>
Operating expenses:				
Cost of sales (exclusive of depreciation and amortization)	379	402	738	842
Selling	415	456	875	914
General, administrative and other operating	469	380	920	832
Affiliates	31	45	82	90
Depreciation and amortization	494	514	987	1,028
Total operating expenses	<u>1,788</u>	<u>1,797</u>	<u>3,602</u>	<u>3,706</u>
Operating income	675	810	1,368	1,525
Other expense (income)—net:				
Interest expense on long-term borrowings—net	162	148	308	299
Other—net	22	(1)	20	—
Total other expense (income)—net	<u>184</u>	<u>147</u>	<u>328</u>	<u>299</u>
Income before income taxes	491	663	1,040	1,226
Income tax expense	186	252	395	466
Net income	<u>\$ 305</u>	<u>\$ 411</u>	<u>\$ 645</u>	<u>\$ 760</u>

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

**QWEST CORPORATION**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
**(UNAUDITED)**

	June 30, 2009	December 31, 2008
	(Dollars in millions)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 906	\$ 233
Accounts receivable—net of allowance of \$53 and \$52, respectively	832	907
Accounts receivable—affiliates	74	127
Deferred income taxes—net	200	203
Prepaid expenses and other	234	241
Total current assets	2,246	1,711
Property, plant and equipment—net	11,012	11,441
Capitalized software—net	859	844
Prepaid pension—affiliate	996	1,047
Other	339	400
Total assets	\$ 15,452	\$ 15,443
LIABILITIES AND STOCKHOLDER'S EQUITY		
Current liabilities:		
Current portion of long-term borrowings	\$ 514	\$ 19
Accounts payable	431	430
Accounts payable—affiliates	104	224
Dividends payable—Qwest Services Corporation	400	400
Accrued expenses and other	874	891
Current portion of post-retirement and other post-employment benefits and other—affiliates	177	179
Deferred revenue and advance billings	402	409
Total current liabilities	2,902	2,552
Long-term borrowings—net of unamortized debt discount and other of \$161 and \$103, respectively	7,832	7,569
Post-retirement and other post-employment benefits and other—affiliates	2,625	2,597
Deferred income taxes—net	1,196	1,262
Other	692	677
Total liabilities	15,247	14,657
Commitments and contingencies (Note 9)		
Stockholder's equity:		
Common stock—one share without par value, owned by Qwest Services Corporation	11,297	11,326
Accumulated deficit	(11,092)	(10,540)
Total stockholder's equity	205	786
Total liabilities and stockholder's equity	\$ 15,452	\$ 15,443

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

**QWEST CORPORATION**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(UNAUDITED)**

	Six Months Ended June 30,	
	2009	2008
	(Dollars in millions)	
Operating activities:		
Net income	\$ 645	\$ 760
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	987	1,028
Deferred income taxes	23	229
Provision for bad debt—net	43	39
Other non-cash charges—net	11	19
Changes in operating assets and liabilities:		
Accounts receivable	35	7
Accounts receivable—affiliates	51	(72)
Prepaid expenses and other current assets	14	29
Accounts payable and accrued expenses and other current liabilities	(16)	(147)
Accounts payable and accrued expenses and other current liabilities—affiliates	(129)	(117)
Deferred revenue and advance billings	(19)	(14)
Other non-current assets and liabilities including affiliates	59	(79)
Cash provided by operating activities	<u>1,704</u>	<u>1,682</u>
Investing activities:		
Expenditures for property, plant and equipment and capitalized software	(542)	(745)
Changes in interest in investments managed by Qwest Services Corporation	(3)	(43)
Other	(7)	7
Cash used for investing activities	<u>(552)</u>	<u>(781)</u>
Financing activities:		
Proceeds from long-term borrowings	738	—
Repayments of long-term borrowings, including current maturities	(14)	(13)
Repayments of long-term borrowings, including current maturities—affiliates	—	(22)
Dividends paid to Qwest Services Corporation	(1,200)	(1,000)
Equity infusions from Qwest Services Corporation	—	231
Other	(3)	4
Cash used for financing activities	<u>(479)</u>	<u>(800)</u>
Cash and cash equivalents:		
Increase in cash and cash equivalents	673	101
Beginning balance	233	292
Ending balance	<u>\$ 906</u>	<u>\$ 393</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 Six Months Ended June 30, 2009**

**(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**

The condensed consolidated balance sheet as of December 31, 2008, which was derived from audited financial statements, and the unaudited interim condensed consolidated financial statements as of and for the three and six months ended June 30, 2009 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. We have evaluated subsequent events through July 29, 2009, the date these financial statements were issued. We have reclassified certain prior year revenue and expense amounts presented in our Quarterly Report on Form 10-Q for the three and six months ended June 30, 2008 to conform to the current period presentation and to the presentation of the full year 2008 results of operations included in our Annual Report on Form 10-K for the year ended December 31, 2008.

In the opinion of management, these statements include all normal recurring adjustments necessary to fairly present our condensed consolidated results of operations, financial position and cash flows as of June 30, 2009 and for all 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, 2008.

The condensed consolidated results of operations for the three and six months ended June 30, 2009 and the condensed consolidated statement of cash flows for the six months ended June 30, 2009 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.

***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, reserves 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 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

**QWEST CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**For the Three and Six Months Ended June 30, 2009**

**(Unaudited)**

**Note 1: Basis of Presentation (Continued)**

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, the impact of an uncertain tax position that is more likely than not of being sustained upon audit by the relevant taxing authority must be recognized at the largest amount that is more likely than not to be sustained. No benefit from an uncertain tax position will be recognized if the position has less than a 50% likelihood of being sustained. Also, interest expense is recognized on the full amount of uncertain tax positions recorded.

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

***Universal Service Funds (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 \$46 million and \$89 million for the three and six months ended June 30, 2009, respectively, and \$51 million and \$100 million for the three and six months ended June 30, 2008, respectively.

***Depreciation and Amortization***

Property, plant and equipment is shown net of accumulated depreciation on our condensed consolidated balance sheets. Accumulated depreciation was \$32.681 billion and \$32.499 billion as of June 30, 2009 and December 31, 2008, respectively.

Capitalized software is shown net of accumulated amortization on our condensed consolidated balance sheets. Accumulated amortization was \$1.521 billion and \$1.448 billion as of June 30, 2009 and December 31, 2008, respectively.

Effective January 1, 2009, we changed our estimates of the average remaining lives of certain copper cable and telecommunications equipment assets. These changes resulted in additional depreciation expense of approximately \$9 million and \$18 million for the three and six months ended June 30, 2009, respectively, compared to the three and six months ended June 30, 2008, and will result in additional depreciation expense of approximately \$36 million for the full year ending December 31, 2009 compared to the year ended December 31, 2008. The additional depreciation for these changes, net of deferred taxes, reduced net income by approximately \$5 million and \$11 million for the three and six months ended June 30, 2009, respectively, and will reduce net income by approximately \$22 million for the full year ending December 31, 2009.

**QWEST CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**For the Three and Six Months Ended June 30, 2009**

**(Unaudited)**

**Note 1: Basis of Presentation (Continued)**

***Recently Adopted Accounting Pronouncements***

Effective January 1, 2009, we adopted Financial Accounting Standards Board ("FASB") Staff Position ("FSP") Financial Accounting Standard ("FAS") 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly" (Accounting Standards Codification ("ASC") 820-10-65). This FSP provides guidelines for ensuring that fair value measurements are consistent with the principles presented in Statement of Financial Accounting Standards ("SFAS") No. 157, "Fair Value Measurements" ("SFAS No. 157") (ASC 820-10). The adoption of this FSP has not had a material effect on our financial position or results of operations.

Effective January 1, 2009, we adopted FSP FAS 115-2 and FAS 124-2, "Recognition and Presentation of Other-Than-Temporary Impairments" (ASC 320-10-65). This FSP provides additional guidance designed to create greater clarity and consistency in accounting for and presenting impairment losses on securities. The adoption of this FSP has not had a material effect on our financial position or results of operations.

**Note 2: Fair Value of Financial Instruments**

Our financial instruments consist of cash and cash equivalents, certain of our current and non-current investments (consisting of auction rate securities and an investment fund), accounts receivable, accounts payable, interest rate hedges and long-term notes including the current portion. The carrying values of cash and cash equivalents, accounts receivable and accounts payable, interest rate hedges, the investment fund, and auction rate securities approximate their fair values.

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 market participants 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 FASB in SFAS No. 157 (ASC 820-1).

# QWEST CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended June 30, 2009

(Unaudited)

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

The table below presents the fair values for certain of our current and non-current investments, 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 June 30, 2009 and December 31, 2008:

	<u>Level</u>	<u>Fair value as of</u>	
		<u>June 30, 2009</u>	<u>December 31, 2008</u>
		<u>(Dollars in millions)</u>	
Assets:			
Auction rate securities	3	\$ 48	\$ 43
Investment fund	3	7	9
Total assets		<u>\$ 55</u>	<u>\$ 52</u>
Liabilities:			
Long-term notes, including the current portion	1 & 2	\$ 7,664	\$ 6,189
Interest rate hedges	3	7	8
Total liabilities		<u>\$ 7,671</u>	<u>\$ 6,197</u>

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

Input Level	Description of Input
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 discounted cash flow model that takes into consideration the interest rate of the securities, the probability that we will be able to sell the securities in an auction or that the securities will be redeemed early, the probability that a default will occur and its severity, a discount rate and other factors.

We determined the fair value of our investment fund based on the asset values of the securities underlying the fund.

# QWEST CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended June 30, 2009

(Unaudited)

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

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 Rate ("LIBOR"). We valued the debt underlying the fair value hedges using projected future cash flows, discounted at mid-market implied forward LIBOR, plus a constant spread above LIBOR determined at the inception of the hedging relationship. We determined these valuations 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 discounted future cash flows using current market interest rates. Unlike the items listed above, our long-term notes including the current portion are reflected on our condensed consolidated balance sheets at original cost net of unamortized discounts and premiums. The carrying value of our long-term notes including the current portion was \$8.306 billion as of June 30, 2009. For additional information, see Note 4—Borrowings.

The table below presents a rollforward of the instruments valued using Level 3 inputs for the six months ended June 30, 2009:

	<u>Instruments Valued Using Level 3 Inputs</u>		
	<u>Auction rate</u>	<u>Investment</u>	<u>Interest rate</u>
	<u>securities</u>	<u>fund</u>	<u>hedges</u>
	<u>(Dollars in millions)</u>		
Balance at January 1	\$ 43	\$ 9	\$ (8)
Transfers into (out of) Level 3	—	—	—
Additions	5	1	—
Dispositions	—	(4)	—
Realized and unrealized losses:			
Included in other (expense) income—net	—	1	—
Included in other comprehensive income	—	—	1
Balance at June 30	<u>\$ 48</u>	<u>\$ 7</u>	<u>\$ (7)</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. These changes are reflected on a net basis in cash flows from investing activities on our condensed consolidated statements of cash flows.

As of June 30, 2009 and December 31, 2008, our investments included auction rate securities of \$48 million and \$43 million, respectively, 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. Auction rate securities are generally long-term debt instruments that provide liquidity through a Dutch auction process that resets the applicable interest rate at pre-determined calendar intervals, generally every 28 days. This mechanism generally allows existing investors to rollover their holdings and continue to own their respective securities or liquidate their

**QWEST CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**For the Three and Six Months Ended June 30, 2009**

**(Unaudited)**

**Note 3: Investments (Continued)**

holdings by selling their securities at par value. Prior to August 2007, QSC invested in these securities for short periods of time as part of its cash management program. However, the uncertainties in the credit markets have prevented QSC and other investors from liquidating holdings of these securities in auctions since the third quarter of 2007. These securities:

- are structured obligations of special purpose reinsurance entities associated with life insurance companies and are referred to as "Triple X" securities;
- currently pay interest every 28 days at one-month LIBOR plus 200 basis points;
- are rated A;
- are insured against loss of principal and interest by two bond insurers. One bond insurer had a credit rating of BBB and the other bond insurer was not rated at June 30, 2009;
- are collateralized by the issuers; and
- mature between 2033 and 2036.

We recorded an immaterial amount of unrealized gains and losses, net of deferred income taxes, on these auction rate securities for the three months ended June 30, 2009 and 2008, and for the six months ended June 30, 2009 and 2008. The cumulative unrealized losses, net of deferred income taxes, related to these securities were \$9 million and \$8 million as of June 30, 2009 and December 31, 2008, respectively. These unrealized losses were recorded in accumulated other comprehensive income, which is included in accumulated deficit in our condensed consolidated balance sheets. The cost basis of these securities was \$62 million as of June 30, 2009 and \$56 million as of December 31, 2008. 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 \$62 million cost basis, in part because the securities are rated investment grade, the securities are fully collateralized and the issuers continue to make required interest payments. 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 or if we believe it is more likely than not that we will be required to sell these securities before their values recover; we would then recognize the portion of the other-than-temporary decline in fair value that is due to credit loss in other expense (income)—net in our condensed consolidated statements of operations. Because we are uncertain as to when the liquidity issues relating to these investments will improve, we continued to classify these securities as non-current as of June 30, 2009.

# QWEST CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended June 30, 2009

(Unaudited)

### Note 4: Borrowings

As of June 30, 2009 and December 31, 2008, our long-term borrowings, net of unamortized discounts and premiums, consisted of the following:

	June 30,	December 31,
	2009	2008
	(Dollars in millions)	
Current portion of long-term borrowings:		
Long-term notes	\$ 500	\$ —
Long-term capital lease and other obligations	14	19
Total current portion of long-term borrowings	514	19
Long-term borrowings:		
Long-term notes	7,806	7,554
Long-term capital lease and other obligations	26	15
Total long-term borrowings—net	7,832	7,569
Total long-term borrowings—net, including current portion	\$8,346	\$ 7,588

We were in compliance with all provisions and covenants of our borrowings as of June 30, 2009.

### New Issuance

In April 2009, we issued approximately \$811 million of 8.375% Senior Notes due 2016. We are using the net proceeds of \$738 million for general corporate purposes, including repayment of indebtedness and funding and refinancing investments in our telecommunication assets.

### Credit Facility

In April 2009, in connection with the addition of a new lender to QCII's revolving credit facility (referred to as the Credit Facility), the amount available to QCII under the Credit Facility increased from \$850 million to \$910 million. In July 2009, in connection with a \$35 million increase in commitment by an existing lender to the Credit Facility, the amount available to QCII under the Credit Facility increased from \$910 million to \$945 million. The Credit Facility is currently undrawn and expires in October 2010. 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

**QWEST CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**For the Three and Six Months Ended June 30, 2009**

**(Unaudited)**

**Note 5: Derivative Financial Instruments (Continued)**

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 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.

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.

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.

We assess quarterly whether each derivative is highly effective in offsetting changes in fair values or cash flows of the hedged item. If we determine that a derivative is not highly effective as a hedge, or if a derivative ceases to be a highly effective hedge, 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 2008, we entered into the interest rate hedges described below as part of our short-term and long-term debt strategies. One objective of our short-term debt strategy is to take advantage of favorable interest rates by swapping floating rate debt to fixed rate debt using cash flow hedges. One objective of our long-term debt strategy is to achieve a more balanced ratio of fixed rate to floating rate debt by swapping a portion of our fixed interest rate debt to floating rate debt through fair value hedges. This decreases our exposure to changes in the fair value of our fixed interest rate debt due to changes in interest rates.

We evaluate counterparty credit risk before entering into any hedge transaction. Thereafter, we continue to closely monitor the financial market and the risk that our counterparties will default on their obligations to us. We are prepared to unwind these hedge transactions if our counterparties' credit risk becomes unacceptable to us.

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. The notes bear interest



# QWEST CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended June 30, 2009

(Unaudited)

### Note 5: Derivative Financial Instruments (Continued)

at a rate per year equal to LIBOR plus 3.25%. These hedges had the economic effect of converting our floating interest rate to fixed interest rates of approximately 6.0% for a term of approximately two years. We designated these interest rate swaps as cash flow hedges. We did not recognize any gain or loss in earnings for hedge ineffectiveness for the six months ended June 30, 2009.

In March 2008, we also entered into interest rate hedges on the outstanding \$500 million aggregate principal amount of our 6.5% Notes due 2017. These hedges had the economic effect of converting our fixed interest rate to a floating interest rate until these notes mature in 2017. We designated these interest rate swaps as fair value hedges. We terminated these hedges in the fourth quarter of 2008.

The cash flow hedges were valued using projected future cash flows, discounted at mid-market implied forward LIBOR. This valuation was determined excluding accrued interest.

The fair value of derivative instruments designated as hedging instruments as of June 30, 2009 is described below:

Asset Derivatives		Liability Derivatives	
Balance sheet location	Fair value	Balance sheet location	Fair value
(Dollars in millions)			
Cash flow hedging contracts	Other current assets \$ —	Other current liabilities	\$ 7

The fair value of derivative instruments designated as hedging instruments as of December 31, 2008 is described below:

Asset Derivatives		Liability Derivatives	
Balance sheet location	Fair value	Balance sheet location	Fair value
(Dollars in millions)			
Cash flow hedging contracts	Other non-current assets \$ —	Other non-current liabilities	\$ 8

For additional information on the fair value of our financial instruments, see Note 2—Fair Value of Financial Instruments.

# QWEST CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended June 30, 2009

(Unaudited)

### Note 5: Derivative Financial Instruments (Continued)

The following table presents the effect of derivative instruments on our condensed consolidated statements of operations for the three and six months ended June 30, 2009 and our condensed consolidated balance sheet as of June 30, 2009:

<u>Derivatives in Cash Flow Hedging Relationships</u>	Three Months Ended	Six Months Ended
	<u>June 30, 2009</u>	<u>June 30, 2009</u>
	(Dollars in millions)	
<b>Interest rate contracts:</b>		
Amount of gain recognized in other comprehensive income on derivative (effective portion), net of deferred taxes of \$— for both periods	\$—	\$ 1
Location of amount reclassified from accumulated other comprehensive income into income (effective portion)	Interest expense—net	Interest expense—net
Amount of loss reclassified from accumulated other comprehensive income into interest expense (effective portion), net of deferred taxes of \$— and \$1, respectively	\$ 1	\$ 2
Location of amount recognized in income on derivative (ineffective portion and amount excluded from effectiveness testing)	Not Applicable	Not Applicable
Amount recognized in income on derivative (ineffective portion and amount excluded from effectiveness testing)	\$—	\$—

### Note 6: Severance

For the three months ended June 30, 2009 and 2008, we recorded severance expenses of \$21 million and \$3 million, respectively. For the six months ended June 30, 2009 and 2008, we recorded severance expenses of \$43 million and \$48 million, respectively. A portion of our severance charges 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 June 30, 2009 and December 31, 2008, our severance liability was \$57 million and \$54 million, respectively. We expect to pay substantially all of the accrued severance charges during the next twelve months.

### Note 7: Tax Matters

During the second quarter of 2009, QCII executed a settlement with the IRS relating to its audit of tax years 2002 and 2003.

### 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

# QWEST CORPORATION

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended June 30, 2009

(Unaudited)

### Note 8: Contribution to QCII Segments (Continued)

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. Consequently, we do not provide our discrete financial information to the CODM on a regular basis.

The following table summarizes revenue for our major products and services for the three and six months ended June 30, 2009 and 2008:

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Operating revenue:				
Data, Internet and video services	\$ 810	\$ 795	\$1,628	\$1,582
Voice services	1,184	1,310	2,405	2,656
Affiliate and other services	469	502	937	993
Total operating revenue	<u>\$2,463</u>	<u>\$2,607</u>	<u>\$4,970</u>	<u>\$5,231</u>

### 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 recorded, or could reasonably anticipate recording, reserves if appropriate to do so.

Throughout this note, 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. Settlement classes have been certified in connection with the settlements of certain of the putative class actions described below where the courts held that the named plaintiffs represented the settlement class they purported to represent.

To the extent appropriate, we have provided reserves for each of the matters described below.

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 and employees with respect to certain of the matters described below, and QCII has been advancing legal fees and costs to many former directors, officers and employees in connection with certain matters described below.

#### KPNQwest Litigation/Investigation

On January 27, 2009, the trustees in the Dutch bankruptcy proceeding for KPNQwest, N.V. (of which QCII was a major shareholder) filed a lawsuit in the federal district court for the District of Colorado alleging violations of the Racketeer Influenced and Corrupt Organizations Act and breach of duty and mismanagement under Dutch law. QCII is a defendant in this lawsuit along with

## QWEST CORPORATION

### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended June 30, 2009

(Unaudited)

#### Note 9: Commitments and Contingencies (Continued)

Joseph P. Nacchio, our former chief executive officer, Robert S. Woodruff, our former chief financial officer and John McMaster, the former president and chief executive officer of KPNQwest. 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 of approximately \$2.4 billion. Plaintiffs also seek treble and punitive damages as well as an award of plaintiffs' attorneys' fees and costs. A lawsuit asserting the same claims that was previously filed in the federal district court for the District of New Jersey was dismissed without prejudice, and that dismissal was affirmed on appeal.

On September 13, 2006, Cargill Financial Markets, Plc and Citibank, N.A. filed a lawsuit in the District Court of Amsterdam, located in the Netherlands, against QCII, KPN Telecom B.V., Koninklijke KPN N.V. ("KPN"), Mr. Nacchio, Mr. McMaster, and other former employees or supervisory board members of QCII, KPNQwest or KPN. The lawsuit alleges that defendants misrepresented KPNQwest's financial and business condition in connection with 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 \$308 million based on the exchange rate on June 30, 2009).

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 allege, among other things, that defendants violated state securities laws in connection with plaintiffs' investments in KPNQwest securities. QCII is a defendant in this lawsuit along with Qwest B.V. (one of QCII's subsidiaries), Mr. Nacchio and Mr. McMaster. The Arizona Superior Court dismissed most of plaintiffs' claims, and plaintiffs voluntarily dismissed the remainder of their claims. Plaintiffs have appealed the court's decision to the Arizona Court of Appeals. Plaintiffs claim to have lost approximately \$9 million in their investments in KPNQwest, and are 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, located in 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.

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

#### Securities Litigation

On January 28, 2009, certain investment companies managed by Munder Capital Management ("Munder Funds")—which were excluded at their request from the settlement class in the Nacchio/Woodruff settlement described below under "Settlement of Consolidated Securities Action"—filed a lawsuit against Messrs. Nacchio and Woodruff alleging that during the time they were affiliated

## QWEST CORPORATION

### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended June 30, 2009

(Unaudited)

#### Note 9: Commitments and Contingencies (Continued)

with QCII, they violated federal securities laws by issuing false and misleading financial reports and statements, falsely inflating revenue and decreasing expenses, creating false perceptions of revenue and growth prospects and employing improper accounting practices. Munder Funds contend that they have incurred losses resulting from their investment in QCII's securities of approximately \$110 million, and they seek compensatory and rescissory damages, pre- and post-judgment interest, costs and attorneys' fees.

#### Other Matters

Several putative class actions relating to the installation of fiber optic cable in certain rights-of-way were filed against QCII on behalf of landowners on various dates and in various courts in California, Colorado, Georgia, Illinois, Indiana, Kansas, Massachusetts, Mississippi, Missouri, Oregon, South Carolina, Tennessee and Texas. For the most part, the complaints challenge QCII's right to install its fiber optic cable in railroad rights-of-way. Complaints in Colorado, Illinois and Texas, also challenge QCII's right to install fiber optic cable in utility and pipeline rights-of-way. The complaints allege that the railroads, utilities and pipeline companies own the right-of-way as an easement that did not include the right to permit QCII to install its fiber optic cable in the right-of-way without the plaintiffs' consent. Most actions (California, Colorado, Georgia, Kansas, Mississippi, Missouri, Oregon, South Carolina, Tennessee and Texas) purport to be brought on behalf of state-wide classes in the named plaintiffs' respective states. The Massachusetts action purports to be on behalf of state-wide classes in all states in which QCII has fiber optic cable in railroad rights-of-way (other than Louisiana and Tennessee), and also on behalf of two classes of landowners whose properties adjoin railroad rights-of-way originally derived from federal land grants. Several actions purport to be brought on behalf of multi-state classes. The Illinois state court action purports to be on behalf of landowners in Illinois, Iowa, Kentucky, Michigan, Minnesota, Nebraska, Ohio and Wisconsin. The Illinois federal court action purports to be on behalf of landowners in Arkansas, California, Florida, Illinois, Indiana, Missouri, Nevada, New Mexico, Montana and Oregon. The Indiana action purports to be on behalf of a national class of landowners adjacent to railroad rights-of-way over which QCII's network passes. 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 November 18, 2008, the court held a hearing to consider final approval of the proposed settlement and the parties are awaiting the court's decision.

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 ("FCC") 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

## QWEST CORPORATION

### NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the Three and Six Months Ended June 30, 2009

(Unaudited)

#### **Note 9: Commitments and Contingencies (Continued)**

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 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. The court has since dismissed or granted summary judgment to QCII on five of the eight claims asserted by plaintiffs. QCII believes the three remaining claims are without merit, and QCII has moved for summary judgment on those claims.

#### **Matters resolved during second quarter, 2009:**

##### **Settlement of Consolidated Securities Action**

Twelve putative class actions purportedly brought on behalf of purchasers of QCII's publicly traded securities between May 24, 1999, and February 14, 2002 were consolidated into a consolidated securities action pending in federal district court in Colorado against QCII and various other defendants. The first of these actions was filed on July 27, 2001. Plaintiffs alleged, among other things, that defendants issued false and misleading financial results and made false statements about QCII's business and investments, including materially false statements in certain of QCII's registration statements. The most recent complaint in this matter sought unspecified compensatory damages and other relief. However, counsel for plaintiffs indicated that the putative class would seek damages in the tens of billions of dollars.

In November 2005, QCII, certain other defendants, and the putative class representatives entered into, and filed with the federal district court in Colorado, a Stipulation of Partial Settlement that settled the consolidated securities action against QCII and certain other defendants (the "QCII settlement"). No parties admit any wrongdoing as part of the QCII settlement. Pursuant to the QCII settlement, QCII deposited approximately \$400 million in cash into a settlement fund. In connection with the QCII settlement, QCII received \$10 million from Arthur Andersen LLP. As part of the QCII settlement, the class representatives and the settlement class they represent are also releasing Arthur Andersen.

The QCII settlement resolved and released the individual claims of the class representatives and the claims of the settlement class they represent against QCII and all defendants except Joseph Nacchio, QCII's former chief executive officer, and Robert Woodruff, QCII's former chief financial officer. In September 2006, the federal district court in Colorado issued an order approving the proposed QCII settlement and certified a class for settlement purposes of purchasers of QCII's publicly traded securities between May 24, 1999 and July 28, 2002, over the objections of Messrs. Nacchio and Woodruff. Messrs. Nacchio and Woodruff then appealed that order to the United States Court of Appeals for the Tenth Circuit. In addressing that appeal, the Tenth Circuit held that the federal district court order overruling Nacchio and Woodruff's objections to the QCII settlement was not sufficiently specific, and it remanded the case to the district court with instructions to consider certain issues and

**QWEST CORPORATION**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**For the Three and Six Months Ended June 30, 2009**

**(Unaudited)**

**Note 9: Commitments and Contingencies (Continued)**

to provide a more detailed explanation for its earlier decision overruling those objections. Subsequent to the remand, a settlement was reached involving the claims of the putative class against Messrs. Nacchio and Woodruff as described below that resulted in the implementation of the QCII settlement.

On August 4, 2008, QCII, Messrs. Nacchio and Woodruff, and the putative class representatives entered into a Stipulation of Settlement (the "Nacchio/Woodruff settlement"). On May 26, 2009, the court approved the Nacchio/Woodruff settlement and certified a class for settlement purposes of purchasers of QCII's publicly traded securities between May 24, 1999 and July 28, 2002. The Nacchio/Woodruff settlement (i) settled the individual claims of the class representatives and the class they represented against Messrs. Nacchio and Woodruff and (ii) resulted in the withdrawal by Messrs. Nacchio and Woodruff of their objections to the QCII settlement and the resolution of their indemnification dispute with QCII arising from the QCII settlement. Under the Nacchio/Woodruff settlement, QCII deposited \$40 million into a settlement fund, and Messrs. Nacchio and Woodruff have contributed a total of \$5 million of insurance proceeds. No parties admit any wrongdoing as a part of the Nacchio/Woodruff settlement.

The QCII settlement and the Nacchio/Woodruff settlement became final on June 26, 2009, at which point QCII's rights pertaining to the amounts deposited into the settlement fund were extinguished. This resulted in a decrease in QCII's other non-current assets and a corresponding decrease in QCII's other non-current liabilities of approximately \$442 million.

**Note 10: Dividends**

During the three and six months ended June 30, 2009, we declared cash dividends to QSC of \$600 million and \$1.200 billion, respectively, and paid cash dividends to QSC of \$570 million and \$1.200 billion, respectively.

## 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 provide data, Internet, video and voice services. We generate revenue from services provided in 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.

Our operations are included in the consolidated operations of our ultimate parent, 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;
- Virtual private network; and
- Voice over Internet Protocol, or VoIP.

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 data and voice 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 ("WAN") products and services, which consist of asynchronous transfer mode, or ATM, and frame relay.

Our analysis presented below is organized to provide the information we believe will be useful for understanding the relevant trends going forward. However, 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.



## 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 future results of operations, cash flows or financial position.

- *Growth in data, Internet and video services.* Revenue from data, Internet and video services represented 33% and 30% of our total revenue for the six months ended June 30, 2009 and 2008, respectively and continues to grow. We also continue to see shifts in the makeup of this revenue as customers move from traditional data, Internet and video products and services to those which use more advanced technologies including broadband services, private line, and video services. Revenue from these growth products and services was 88% of our total data, Internet and video revenue for the six months ended June 30, 2009. The revenue increases from our growth products and services have outpaced revenue declines from certain data and Internet services such as our traditional WAN services.

We also continue to focus on increasing subscribers of our broadband services, particularly with respect to our consumer and small business customers. We reached 2.9 million broadband subscribers at June 30, 2009 compared to 2.6 million at June 30, 2008. 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 ("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 maturing market where a significant portion of consumers already have broadband services. We now expect the net number of our broadband subscriber additions in 2009 will be comparable to our net additions in 2008; however, we are experiencing intense broadband competition and price compression.

- *Continuing loss of access lines.* Our revenue has been, and we expect it will continue to be, adversely affected by access line losses. Intense competition, including product substitution, continues to drive our access line losses. For example, many consumers are substituting cable, wireless and VoIP for traditional voice telecommunications services. This has increased the number and type of competitors within our industry and has decreased our market share. Additionally, we believe that intensified competition, wireless substitution and declining general economic conditions contributed to an acceleration of our access line losses in recent quarters. 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 access line losses.
- *Product bundling and 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 voice services with other services such as broadband, video, long-distance and wireless. 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. 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.
- *Greater 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 employee attrition, we have reduced our workforce and employee-related

costs (net of severance) while achieving operational efficiencies and improving processes through automation.

- Pension and post-retirement benefits expenses.*** QCII is required to recognize on its condensed 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 the end 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. In 2008 we recognized combined net periodic income, as pension income exceeded post-retirement benefit expense for the year. However, during 2008 QCII experienced significant losses on its pension and post-retirement benefit plan assets, which have significantly impacted the pension and post-retirement benefits expenses we are recording in 2009. Changes to QCII's assumptions in future periods may further increase or decrease our expected combined net periodic expenses beyond 2009.

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

The following table summarizes our results of operations for the three and six months ended June 30, 2009 and 2008 and the number of employees as of June 30, 2009 and 2008:

	Three Months Ended June 30,				Six Months Ended June 30,			
	2009	2008	Increase/ (Decrease)	% Change (Dollars in millions)	2009	2008	Increase/ (Decrease)	% Change
Operating revenue	\$2,463	\$2,607	\$ (144)	(6)%	\$ 4,970	\$ 5,231	\$ (261)	(5)%
Operating expenses	1,788	1,797	(9)	(1)%	3,602	3,706	(104)	(3)%
Operating income	675	810	(135)	(17)%	1,368	1,525	(157)	(10)%
Other expense (income)—net	184	147	37	25%	328	299	29	10%
Income before income taxes	491	663	(172)	(26)%	1,040	1,226	(186)	(15)%
Income tax expense	186	252	(66)	(26)%	395	466	(71)	(15)%
Net income	<u>\$ 305</u>	<u>\$ 411</u>	<u>\$ (106)</u>	<u>(26)%</u>	<u>\$ 645</u>	<u>\$ 760</u>	<u>\$ (115)</u>	<u>(15)%</u>
Employees (as of June 30)					29,150	32,242	(3,092)	(10)%

### Operating Revenue

Operating revenue decreased primarily due to continued access line losses and declining revenue from our traditional WAN services. The decrease in overall revenue was partially offset by increased revenue associated with our growth products and services.

The following table summarizes our operating revenue for the three and six months ended June 30, 2009 and 2008:

	Three Months Ended June 30,				Six Months Ended June 30,			
	2009	2008	Increase/ (Decrease)	% Change (Dollars in millions)	2009	2008	Increase/ (Decrease)	% Change
Operating revenue:								
Data, Internet and video services	\$ 810	\$ 795	\$ 15	2%	\$1,628	\$1,582	\$ 46	3%
Voice services	1,184	1,310	(126)	(10)%	2,405	2,656	(251)	(9)%
Affiliate and other services	469	502	(33)	(7)%	937	993	(56)	(6)%
Total operating revenue	<u>\$2,463</u>	<u>\$2,607</u>	<u>\$ (144)</u>	<u>(6)%</u>	<u>\$4,970</u>	<u>\$5,231</u>	<u>\$ (261)</u>	<u>(5)%</u>

The following table summarizes our total broadband and video subscribers and access lines by customer channel as of June 30, 2009 and 2008:

	June 30,			
	2009	2008	Increase/ (Decrease)	% Change
	(in thousands)			
Total broadband subscribers	<u>2,884</u>	<u>2,647</u>	<u>237</u>	<u>9%</u>
Total video subscribers	<u>833</u>	<u>666</u>	<u>167</u>	<u>25%</u>
Access lines:				
Business markets	2,526	2,713	(187)	(7)%
Mass markets	7,288	8,266	(978)	(12)%
Wholesales markets	1,075	1,210	(135)	(11)%
Total access lines	<u>10,889</u>	<u>12,189</u>	<u>(1,300)</u>	<u>(11)%</u>

In addition to the specific items discussed below, we believe declining general economic conditions negatively impacted our revenue.

### Data, Internet and Video Services

Data, Internet and video services revenue increased primarily due to an increase in broadband subscribers and, to a lesser extent, an increase in video subscribers as of June 30, 2009 compared to June 30, 2008. The increase in broadband services revenue resulting from an increase in subscribers was partially offset by rate discounts. Private line services revenue also increased due to higher volumes. These revenue increases were partially offset by a decrease in our traditional WAN services revenue due to lower volumes.

### Voice Services

Voice services revenue decreased primarily due to lower local voice services revenue, which was driven by access line losses resulting from the competitive pressures described in "Business Trends" above. Local voice services revenue was impacted by these competitive pressures as customers disconnected primary and additional lines. Access and local voice services revenue declined due to access line loss and a declining demand for unbundled network elements for the six months ended June 30, 2009 compared to the same period in 2008.

## Affiliate and Other Services Revenue

Affiliate services revenue decreased primarily due to reduced support associated with an affiliate's winding down of its wireless business as we transition to selling Verizon Wireless products and services. In addition, we had reduced support associated with an affiliate's winding down of its video and data products and services. These decreases in affiliate services were partially offset by an increase in services we provided to support an affiliate's data and Internet product offerings.

We estimate that the profit from affiliate services was approximately \$70 million and \$100 million, before income taxes, for the three months ended June 30, 2009 and 2008, respectively, and \$160 million and \$210 million, before income taxes, for the six months ended June 30, 2009 and 2008, respectively.

## Operating Expenses

The following table provides further detail regarding our total operating expenses for the three and six months ended June 30, 2009 and 2008:

	Three Months Ended June 30,				Six Months Ended June 30,			
	2009	2008	Increase/ (Decrease)	% Change	2009	2008	Increase/ (Decrease)	% Change
(Dollars in millions)								
Cost of sales (exclusive of depreciation and amortization):								
Employee-related costs	\$ 259	\$ 270	\$ (11)	(4)%	\$ 513	\$ 602	\$ (89)	(15)%
Other	120	132	(12)	(9)%	225	240	(15)	(6)%
Total cost of sales	379	402	(23)	(6)%	738	842	(104)	(12)%
Selling:								
Employee-related costs	245	268	(23)	(9)%	519	534	(15)	(3)%
Marketing, advertising and external commissions	109	111	(2)	(2)%	219	235	(16)	(7)%
Other	61	77	(16)	(21)%	137	145	(8)	(6)%
Total selling	415	456	(41)	(9)%	875	914	(39)	(4)%
General, administrative and other operating:								
Employee-related costs	175	112	63	56%	325	236	89	38%
Taxes and fees	99	61	38	62%	197	176	21	12%
Real estate and occupancy costs	66	74	(8)	(11)%	136	152	(16)	(11)%
Other	129	133	(4)	(3)%	262	268	(6)	(2)%
Total general, administrative and other operating	469	380	89	23%	920	832	88	11%
Affiliates	31	45	(14)	(31)%	82	90	(8)	(9)%
Depreciation and amortization	494	514	(20)	(4)%	987	1,028	(41)	(4)%
Total operating expenses	<u>\$1,788</u>	<u>\$1,797</u>	<u>\$ (9)</u>	(1)%	<u>\$3,602</u>	<u>\$3,706</u>	<u>\$ (104)</u>	(3)%

### **Cost of Sales (exclusive of depreciation and amortization)**

Employee-related costs decreased for the three and six months ended June 30, 2009 as compared to the same period in 2008 primarily due to lower salaries, wages and benefits related to employee reductions in our network operations. In addition, severance expense decreased for the six months ended June 30, 2009 and increased for the three months ended June 30, 2009 compared to the same periods in 2008 due to the timing of when employee reductions occurred.

Other cost of sales decreased primarily due to lower network expense and professional fees as a result of our continued focus on managing costs associated with operating and maintaining our network.

### **Selling Expenses**

Employee-related costs decreased due to lower salaries, wages and benefits related to employee reductions in our sales organization for the three and six months ended June 30, 2009 as compared to the same period in 2008. This was partially offset by severance expenses for both the three and six months ended June 30, 2009 as compared to the same period in 2008.

Marketing, advertising and external commissions decreased due to reduced spending associated with media, direct mail, and sponsorships as well as reductions in agency fees.

Other expenses decreased primarily due to lower professional fees as a result of a favorable rate change in credit processing fees and other cost savings initiatives which were partially offset by litigation related losses recorded in the first quarter of 2009.

### **General, Administrative and Other Operating Expenses**

Employee-related costs increased primarily due to increased pension and post-retirement benefits expense. These benefits expenses are based on several assumptions, including among other things, discount rates and expected rates of return on plan assets that are set at the beginning of each year. In 2008 we recognized combined net periodic benefits income, as pension income exceeded post-retirement benefit expense for the year. However, during 2008 QCII experienced significant losses on its pension and post-retirement benefit plan assets, which have significantly impacted the pension and post-retirement benefits expenses we are recording in 2009.

We now expect to recognize approximately \$205 million in combined net periodic benefits expense for 2009 as compared to combined net periodic benefits income of \$13 million for 2008. This expected total combined net benefits expense for 2009 is \$33 million more than the amount we previously disclosed, due primarily to adjustments to our estimates of the fair value of certain private-equity and alternative investments held by our plan trusts that were estimated based on previously available preliminary information at December 31, 2008. Of the annual \$33 million change for 2009, \$17 million has been reflected in the three months ended June 30, 2009 and is included in employee-related costs. Changes to QCII's assumptions at the end of 2009 may increase or decrease our expected combined net periodic benefits expenses beyond 2009.

Taxes and fees increased as a result of a \$40 million favorable property tax settlement and other favorable adjustments in the second quarter of 2008. These increases were partially offset by lower USF charges resulting from continued access line erosion and a decrease in property taxes.

Real estate and occupancy costs decreased primarily due to lower rent expense and fuel costs.

### **Affiliates Expenses**

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

Affiliate expenses decreased primarily due to reduced insurance costs driven by premium discounts and refunds partially offset by increases in wholesale Internet access in support of our broadband business.

### Depreciation and Amortization

The following table provides detail regarding depreciation and amortization expense:

	Three Months Ended June 30,				Six Months Ended June 30,			
	2009	2008	Increase/ (Decrease)	% Change	2009	2008	Increase/ (Decrease)	% Change
	(Dollars in millions)							
Depreciation and amortization:								
Depreciation	\$438	\$463	\$ (25)	(5)%	\$877	\$ 927	\$ (50)	(5)%
Amortization	56	51	5	10%	110	101	9	9%
Total depreciation and amortization	<u>\$494</u>	<u>\$514</u>	<u>\$ (20)</u>	<u>(4)%</u>	<u>\$987</u>	<u>\$1,028</u>	<u>\$ (41)</u>	<u>(4)%</u>

Depreciation expense decreased due to lower capital expenditures and the changing mix of our investment in property, plant and equipment since 2002. If our capital expenditures remain approximately the same and 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 for the three and six months ended June 30, 2009 compared to the same periods ended June 30, 2008 due to an increase in internally developed capitalized software used to support our operations.

Effective January 1, 2009, we changed our estimates of the average remaining economic lives of certain copper cable and telecommunications equipment assets. These changes resulted in additional depreciation expense of approximately \$9 million and \$18 million for the three and six months ended June 30, 2009, respectively, compared to the three and six months ended June 30, 2008 and will result in additional depreciation expense of approximately \$36 million for the full year ending December 31, 2009 compared to the year ended December 31, 2008. The additional depreciation for these changes, net of deferred taxes, reduced net income by approximately \$5 million and \$11 million for the three and six months ended June 30, 2009, respectively, and will reduce net income by approximately \$22 million for the full year ending December 31, 2009.

## Other Consolidated Results

The following table provides detail regarding other expense (income)—net and income tax expense:

	Three Months Ended June 30,				Six Months Ended June 30,			
	2009	2008	Increase/ (Decrease)	% Change (Dollars in millions)	2009	2008	Increase/ (Decrease)	% Change
Other expense (income)—net:								
Interest expense on long-term borrowings—net	\$162	\$148	\$ 14	9%	\$308	\$299	\$ 9	3%
Other—net	22	(1)	23	nm	20	—	20	nm
Total other expense (income)—net	<u>\$184</u>	<u>\$147</u>	<u>\$ 37</u>	25%	<u>\$328</u>	<u>\$299</u>	<u>\$ 29</u>	10%
Income tax expense	\$186	\$252	\$ (66)	(26)%	\$395	\$466	\$ (71)	(15)%

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 increased due to increased debt levels as a result of our debt issuance in April 2009, but was partially offset by decreasing interest rates on floating rate notes.

Other—net includes, among other things, interest income, income tax penalties, other interest expense (such as interest on income taxes), and gains and losses related to fair value interest rate hedges. Other—net increased due to higher tax related interest for the three and six months ended June 30, 2009 compared to the three and six months ended June 30, 2008. We expect this tax related interest to reverse in the third quarter of 2009.

### Income Tax Expense

The effective income tax rate is the provision for income taxes as a percentage of income before income taxes. Our effective income tax rate was 38% for the three months ended June 30, 2009 and 2008 and 38% for the six months ended June 30, 2009 and 2008.

## Liquidity and Capital Resources

We are a wholly owned subsidiary of QSC, which is wholly owned by 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 and on our access to capital markets and changes in the financial market's perception of us. QCII and its consolidated subsidiaries had total borrowings of \$14.123 billion and \$13.555 billion at June 30, 2009 and December 31, 2008, 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***

At June 30, 2009, we held cash and cash equivalents totaling \$906 million, and QCII had \$910 million available under its currently undrawn revolving credit facility (referred to as the Credit Facility). 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.

During the 12 months ended June 30, 2009, our net cash generated by operating activities totaled \$3.501 billion. Although our revenue has been decreasing, we believe that we will be able to continue to control costs to keep them aligned with revenue and therefore expect that we will continue to generate cash from operating activities sufficient to fund our financing and investing activities. For the coming 12 months, our expected financing and investing cash needs include capital expenditures (anticipated to be approximately \$1.3 billion or less in 2009), \$500 million of debt maturing in June 2010 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 moderate portion 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.

At June 30, 2009, our current liabilities exceeded our current assets by \$656 million. Our working capital deficit improved as compared to our working capital deficit at December 31, 2008 due to earnings before depreciation and amortization and proceeds on long-term debt, which were partially offset by capital expenditures, non-current debt reclassified to current debt and dividends declared to QSC.

We continue to look for opportunities to improve our capital structure by reducing debt and interest expense. 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. Even though we were able to issue new debt financing in April, the unstable credit markets and the decline in the 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 above, 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 \$500 million maturing in 2010, \$825 million maturing in 2011 and \$1.500 billion maturing in 2012. We believe that we will continue to have access to capital markets to refinance our debt as necessary. Even though we were able to issue new debt financing in April, the unstable credit markets and the decline in the 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.

In July 2009, in connection with a \$35 million increase in commitment by an existing lender to the Credit Facility, the amount available to QCII under the Credit Facility increased from \$910 million to



\$945 million. The Credit Facility is subject to certain restrictions as described below, is currently undrawn and expires in October 2010. The Credit Facility has 13 lenders with commitments ranging from \$15 million to \$160 million. 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 securities-related actions 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 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.

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) if:

- revenue and cash provided by operations significantly decline;
- poor economic conditions continue to persist;
- competitive pressures increase;
- we are required to contribute a material amount of cash to QCII's pension or post-retirement benefit plans; 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 \$745 million at

December 31, 2008. Cash funding requirements are significantly impacted by earnings on investments, the applicable discount rate at the end of each year and funding laws and regulations. As a result, it is difficult to determine future funding requirements with a high level of precision. Based on elections QCII will make in 2010 relating to, among other things, the method of determining discount rates, and subject to any changes in funding laws and regulations, it may be required to make cash contributions to the plan in the range of \$0 to \$300 million in 2010. If the elections that QCII makes do not require a contribution in 2010, it is highly likely that a contribution will be required in 2011. The amount of any required contributions in 2011 and beyond will be dependant upon earnings on investments, discount rates and funding laws and regulations. If a contribution is made in 2010, it may reduce required contributions after 2010.

Our employees participate in the QCII pension 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 their pension contribution.

### Post-Retirement Benefits

Certain of QCII's post-retirement health care and life insurance benefits plans are unfunded. However, a trust has been established to help cover the health care costs of retirees who are former occupational employees. As of December 31, 2008, the fair value of the trust assets was \$915 million and QCII believed that the trust assets would be adequate to provide continuing reimbursements for its occupational post-retirement health care costs for approximately five years assuming that the trust's current asset allocation remains the same and the assets earn an expected long-term rate of return of 8.5%. Thereafter, covered benefits for its eligible retirees who are former occupational employees will be paid directly by QCII. This five year period could be substantially shorter depending on returns on plan assets, projected benefit payments and future changes in benefit obligations; for instance, if QCII assumes that the rate of return on trust assets is zero and benefit reimbursements remain at projected levels, the trust would still be exhausted in approximately five years, but if QCII assumes that the rate of return on trust assets were zero and benefit reimbursements increase by 20%, the trust assets could be exhausted in three years.

Our 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 their post-retirement contribution.

### Historical View

The following table summarizes cash flow activities for the six months ended June 30, 2009 and 2008:

	Six Months Ended June 30,			
	2009	2008	Increase/ (Decrease)	% Change
	(Dollars in millions)			
Cash flows:				
Provided by operating activities	\$1,704	\$1,682	\$ 22	1%
Used for investing activities	552	781	(229)	(29)%
Used for financing activities	479	800	(321)	(40)%

### Operating Activities

Cash provided by operating activities has remained relatively flat.

## **Investing Activities**

Cash used for investing activities decreased primarily due to lower capital expenditures and lower net purchases of investments in securities managed by QSC.

## **Financing Activities**

Cash used for financing activities decreased primarily due to our issuance of \$811 million of Senior Notes in April 2009, which resulted in net proceeds of \$738 million.

We paid cash dividends of \$1.200 billion and \$1.000 billion for the six months ended June 30, 2009 and 2008, respectively. We may 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 June 30, 2009.

## ***Letters of Credit***

We maintain letter of credit arrangements with various financial institutions for up to \$110 million. As of June 30, 2009, we had outstanding letters of credit of approximately \$55 million.

## ***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 currently use derivative financial instruments to manage our interest rate risk exposure and we may continue to employ them in the future.

## **Near-Term Maturities**

As of June 30, 2009, we had \$500 million of long-term notes maturing in the subsequent 12 months. We would be exposed to changes in interest rates at any time that we choose to refinance any of this debt. A hypothetical increase of 100 basis points in the interest rate on a refinancing of the entire current portion of long-term notes would decrease quarterly pre-tax earnings by approximately \$1 million.

## **Floating-Rate Debt**

One objective of our short-term debt strategy is to take advantage of favorable interest rates by effectively converting floating rate debt to fixed rate debt using interest rate swaps. As of June 30, 2009 and December 31, 2008, we had \$750 million of floating-rate debt outstanding, of which \$250 million was exposed to changes in interest rates. This exposure is linked to the London Interbank Offered Rate, or LIBOR. A hypothetical increase of 100 basis points in LIBOR relative to the \$250 million of floating-rate debt that is exposed to changes in interest rates would decrease quarterly pre-tax earnings by less than \$1 million.

## **Investments**

As of June 30, 2009, our cash and investments managed by QSC included \$904 million invested in highly liquid cash-equivalent instruments, \$48 million invested in auction rate securities and \$7 million in an investment fund. As interest rates change, so will the interest income derived from these instruments. Assuming that these investment balances were to remain constant, a hypothetical decrease of 100 basis points in interest rates would decrease quarterly pre-tax earnings by approximately \$2 million.

## **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 six months ended June 30, 2009, when compared to the disclosures provided in our Annual Report on Form 10-K for the year ended December 31, 2008.

## **Website Access and Important Investor Information**

Our website address is [www.qwest.com](http://www.qwest.com), and we routinely post important investor information in the "Investor Relations" section of our website at [www.qwest.com/about/investor](http://www.qwest.com/about/investor). 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 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.

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 June 30, 2009. 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 second quarter of 2009 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 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 product bundling and packaging and QCII's and our continuing focus on customer service. However, we may not be successful in these efforts. We may not be able to distinguish our 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 services 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 current recession in the United States and the recent financial crisis affecting the banking system and financial markets, 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 to recent turmoil in the credit markets and the continued decline in the economy, 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 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, such as broadband, wireless, video and VoIP 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 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 securities-related matters pending against QCII, including 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 securities-related matters, including the KPNQwest matters, present material and significant risks to QCII and us. In the aggregate, the plaintiffs in the KPNQwest matters seek 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 state and federal regulation. Interstate communications (including international communications that originate or terminate in the U.S.) are regulated by the Federal Communications Commission or FCC, pursuant to the Communications Act of 1934, as amended by the Telecommunications Act of 1996, and other laws. Intrastate communications are regulated by state utilities commissions pursuant to state utility laws. Generally, we must obtain and maintain certificates of authority from the FCC and regulatory bodies in most states where we offer regulated services and must obtain prior regulatory approval of rates, terms and conditions for regulated services, where required. 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. A number of state legislatures and state utility commissions 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. At the same time, some of the changes at both the state and federal level may have the potential effect of reducing some regulatory protections, including having FCC-approved



tariffs that include rates, terms and conditions. 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 2009 the state utility commissions in Arizona, New Mexico and Minnesota will be considering whether to renew the price cap plans that govern the rates that we charge in each of these states. 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"). 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 June 30, 2009, our consolidated debt was approximately \$8.3 billion, which was included in QCII's consolidated debt of approximately \$14.1 billion as of that date. Approximately \$6.4 billion of QCII's debt, which includes approximately \$2.8 billion of our debt obligations, comes due over the next three years. The \$6.4 billion amount also includes \$1.265 billion of QCII's 3.50% Convertible Senior Notes due 2025 (referred to as the 3.50% Convertible Senior Notes), which QCII may elect to redeem at any time on or after November 20, 2010 and holders may require QCII to repurchase for cash on November 15, 2010. In addition, holders of these 3.50% Convertible Senior Notes may also elect to convert the principal of their notes into cash during periods when specified, market-based conversion requirements are met. 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, QCII has \$193 million of potential stock repurchases remaining under its previously disclosed stock repurchase program, and 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 purchase its common stock or 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 recent turmoil in the credit markets and the continued decline in the economy, 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) if revenue and cash provided by operations decline, if economic conditions continue to weaken, if competitive pressures increase, if holders of the 3.50% Convertible Senior Notes elect to convert their notes because market-based conversion provisions are met or require QCII to repurchase their notes

for cash on November 15, 2010, if QCII or we are required to contribute a material amount of cash to QCII's pension or other post-retirement benefit plans 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 \$945 million revolving credit facility (referred to as the 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 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 securities-related actions 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 stockholders' equity balance, 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 under these plans. 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 may be required to make cash contributions to this plan as early as 2010. Future material cash contributions, if any, could have a negative impact on QCII's liquidity by reducing its cash flows which in turn could affect our liquidity.

In addition, QCII's condensed consolidated balance sheets indirectly reflect the value of all plan assets and benefit obligations under these plans. The accounting for employee benefit plans is complex, and significant increases in QCII's benefit obligations or significant decreases of the value of plan assets can occur without necessarily impacting QCII's net income in the short term. In addition, QCII's benefit obligations could increase significantly if it needs to unfavorably revise the assumptions it used to calculate the obligations. The value of QCII's plan assets was several times larger than QCII's stockholders' equity as of December 31, 2007. However, asset values decreased significantly in 2008, which caused QCII's previous stockholders' equity position to become a deficit position as of December 31, 2008. Stockholders' equity or deficit is one of several measures used by certain customers and vendors, among others, to evaluate a company's financial condition. As such, QCII's current stockholders' deficit position or any future increases in its stockholders' deficit could adversely impact QCII's competitiveness in obtaining favorable purchase arrangements and make it more challenging to compete for certain sales contracts, among other things.

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

***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, 2008, 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, or IRS, 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.

In April 2008, QCII received from the IRS proposed adjustments on several issues for the 2004 and 2005 audit cycle. Based on QCII's and our evaluation of the IRS's positions reflected in the proposed adjustments, we have not recorded a material adjustment of our unrecognized tax benefits. However, there can be no assurance that QCII and the IRS will reach settlements on any of these issues or that, if QCII does reach settlements, the terms will be favorable to us.

Because prior to 1999 we were a member of affiliated groups filing consolidated U.S. federal income tax returns, we could be severally liable for tax examinations and adjustments not directly applicable to us or to current members of the QCII affiliated group. 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.

***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.

Exhibit Number	Description
(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 <sup>7</sup> / 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).
(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).

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<b>Exhibit Number</b>	<b>Description</b>
(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).
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. WILLIAM JOHNSTON

**R. William Johnston**  
*Senior Vice President, Controller and  
Chief Accounting Officer  
(Chief Accounting Officer and  
Duly Authorized Officer)*

July 29, 2009





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

	Six Months Ended June 30,	Years Ended December 31,				
	2009	2008	2007	2006	2005	2004
Income from continuing operations before income taxes, discontinued operations and cumulative effect of changes in accounting principles	\$1,040	\$2,267	\$2,440	\$1,882	\$1,628	\$1,871
Add: estimated fixed charges	345	671	682	700	700	686
Add: estimated amortization of capitalized interest	5	12	10	10	12	12
Less: interest capitalized	(4)	(14)	(12)	(12)	(10)	(12)
Total earnings available for fixed charges	<u>\$1,386</u>	<u>\$2,936</u>	<u>\$3,120</u>	<u>\$2,580</u>	<u>\$2,330</u>	<u>\$2,557</u>
Estimate of interest factor on rentals	\$ 33	\$ 68	\$ 62	\$ 72	\$ 82	\$ 75
Interest expense, including amortization of premiums, discounts and debt issuance costs(1)	308	589	608	616	608	599
Interest capitalized	4	14	12	12	10	12
Total fixed charges	<u>\$ 345</u>	<u>\$ 671</u>	<u>\$ 682</u>	<u>\$ 700</u>	<u>\$ 700</u>	<u>\$ 686</u>
Ratio of earnings to fixed charges	4.0	4.4	4.6	3.7	3.3	3.7

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

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

**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: July 29, 2009

/s/ EDWARD A. MUELLER

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**Edward A. Mueller**  
*Chief Executive Officer*

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CERTIFICATION OF 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: July 29, 2009

/s/ JOSEPH J. EUTENEUER

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**Joseph J. Euteneuer**  
*Executive Vice President and Chief Financial Officer*

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CERTIFICATION OF 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 June 30, 2009, 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: July 29, 2009

By: /s/ EDWARD A. MUELLER

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**Edward A. Mueller**  
*Chief Executive Officer*

Dated: July 29, 2009

By: /s/ JOSEPH J. EUTENEUER

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**Joseph J. Euteneuer**  
*Executive Vice President and Chief Financial Officer*

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