Statement of John Legere

Chief Executive Officer of Global Crossing

before the

U.S. Senate
Committee on Commerce, Science & Transportation

July 30, 2002

Chairman Hollings and members of the Committee, thank you for inviting us here today to discuss the state of the telecommunications industry. We want to commend you and this Committee for holding a hearing on the critical issue of how the industry's financial health can be restored. This hearing will make a significant contribution to the continuing public dialogue on how we can ensure that the communications infrastructure on which the American people have come to rely is not compromised while the industry makes its way through a period of transition. By holding this hearing, you are sending a positive signal to the financial markets and to the public that Congress is confident that our Nation's telecommunications companies will weather the financial turbulence that we face and that government and the private sector can work together to address the issues in a cooperative and constructive manner.

Despite the much-publicized economic problems of the telecommunications sector, we should not lose sight of the fact that our country has the world's most sophisticated and advanced communications infrastructure and services. Propelled by our enterprising culture and funded by private capital, America's communications companies have created networks that are unparalleled anywhere in the world -- networks that are critical to maintaining our Nation's security and our leadership in the world economy. Every day, Americans are able to reap the substantial benefits of innovation, efficiency and competition that are the product of these investments.

Global Crossing and its thousands of employees are proud participants in this competitive market. We have completed a global fiber optic network that spans 101,000 route miles. We provide some of the world's most advanced telecommunications services to tens of thousands of customers, both in the United States and abroad. For our company, for our employees and, most of all, for every one of our customers, which include many of the largest telecommunications carriers in the world, we ask that this Committee and the Congress do what they can to ensure that competition in the telecommunications industry remains healthy. Ensuring that the industry remains strong and competitive is vital to delivering the innovation and cost efficiencies on which the global economy depends.

We are here today because America's telecommunications industry is threatened by a financial crisis of enormous and unexpected proportions. I hope to share some observations on the sources of this crisis and on how the industry can best survive it. Global Crossing believes that government can play an important role in helping those segments of the communications industry that are in a state of turmoil to recover. Today's hearing is part of our collective opportunity to restore confidence and rebuild the industry.

Given the expressed interests and responsibilities of this Committee, today I intend to address the following: (i) the formation and growth of Global Crossing; (ii) the profound changes in the telecommunications industry, which began in mid-2001, and have brought us to where we are today; (iii) the status of the various governmental inquiries into Global Crossing; (iv) Global Crossing's performance since it filed for bankruptcy on January 28 of this year; and (v) our vision for the future.

I believe that the industry-wide crisis we are experiencing is a product of the interplay among the overall business environment, changing patterns in the supply and demand for network capacity, marketplace perceptions, access to capital and the regulatory environment. These are among the principal industry-wide factors that have caused not only Global Crossing, but also many other companies, to declare bankruptcy within the past 15 months. The pandemic nature of the problem we are facing is demonstrated all-too-clearly by the broad range of telecommunications companies that are now in bankruptcy: they are U.S.-based, as well as international; they own subsea cables, as well as terrestrial systems; they provide long distance services, as well as local access; and they are built on wireless, as well as wireline, technologies.

It is important to emphasize that despite the popular perception that this industry's problems stem from alleged accounting irregularities at a handful of companies, the turmoil we are experiencing is far more complex and more fundamental than the media have led many to believe. Allegations of accounting irregularities properly need to be addressed and may play larger or smaller roles in the difficulties faced by particular companies. Only by understanding the fundamental business factors underlying today's crisis, however, can we all work together to restore the strength of this vital sector.

Formation and Growth of Global Crossing

Global Crossing was created by visionaries who saw an unmet need in the marketplace for an integrated global high-capacity, fiber-optic network under common control. Throughout the history of the telecommunications industry, international traffic had been handed off, from one national carrier to another. As the world entered the age of the Internet, some saw that these legacy networks had neither the capacity nor the functionality to provide adequately for the envisioned Internet-based services. The vision of the founders of Global Crossing was to facilitate, in a more cost-effective manner, the worldwide transport of the surging traffic flows stimulated by the emergence of the Internet.

Global Crossing was launched in 1997 and became a publicly traded company in 1998. The founders of the Company successfully raised substantial amounts of private capital, capital that was essential to Global Crossing's ability to compete with the huge incumbent players (such as, AT&T) and to the construction of a new fiber-optic network that reached most of the world. Based on the widespread belief in multiple independent forecasts of rapid growth in demand for data services, the capital markets supported the project and construction was completed in record time.

Today, as a result of these efforts, Global Crossing has 101,000 route miles of fiber worldwide, fully operational in 220 cities in 27 countries. In addition, the Company has built a large and loyal customer base of public and private entities of all sizes. Our customers range from Kay Bee Toy Stores, with hundreds of stores worldwide, to the British Foreign Commonwealth Office, with over 240 embassies around the globe. Just last week, we announced that we are now linking research telescopes around Europe over our fiber-optic network, allowing research institutions worldwide to advance the science of astronomy. We connect thousands of financial institutions, completing millions of transactions every day over our network.

Our backbone network makes it possible for Americans to phone their relatives and friends in Europe, Asia, Latin America and Australia for dramatically lower costs because those calls can be transmitted over our fiber-optic backbone. And, our network is an important backbone for the Internet, enabling people and businesses to communicate in ways we simply could not have imagined just a decade ago. Despite our Chapter 11 filing and the substantial cost restructuring that we have undertaken, the size and reliability of our network continues to attract some of the world's most important companies, financial institutions, and governments as customers. As a major supplier of wholesale capacity and services, our network supports nearly every major carrier in the world.

As our operations have continued without interruption, even as we proceed with our Chapter 11 reorganization, we are fortunate to have lost very few of our customers. We are enormously grateful for the loyalty of the thousands of customers who have understood that the value of Global Crossing's services was not diminished simply because we had to restructure our finances. That new customers are willing to trust us with their critical communications needs validates the vision of Global Crossing's founders and gives us confidence for the future. Our experience suggests that continuing to focus on customers and service is essential if the industry is to emerge from the current crisis with renewed vigor.

Although we are a global concern, the vast majority of our customers and most of our employees reside in the United States. Our corporate headquarters are in the United States and we have network operations centers here. Global Crossing is an integral part of the Nation's vital communications infrastructure, and we are doing everything we can to keep it that way. Our future as a company depends on it.

Changes in the Telecommunications Industry

The Committee has asked how we got to where we are today. To answer that question, we need to take ourselves back to how the telecommunications world looked just a few short years ago, when optimism – and demand forecasts – appeared nearly unbounded. Throughout the late 1990s and well into 2001, the telecommunications industry and those in the financial world who analyzed the industry foresaw an unending appetite for additional bandwidth capacity. Growth of Internet usage was astonishing, posting gains of several hundred percent a year, increases that were forecast to continue for some time, both in the United States and around the world. Enterprise customers were moving toward feature-rich, IP (Internet Protocol)-based networks of just the sort that we have built at Global Crossing. Many observers foresaw a world in which graphics, music and movies, with other gigabit-rich content, would flow directly to the home, and where new applications – games, virtual reality, distributed computing – would consume huge quantities of bandwidth.

In part, these expectations relied significantly on overcoming the last hurdle in the telecommunications world: the last mile. High-bandwidth intercity and international networks were constructed to facilitate commerce and satisfy consumer demand. Consumers and businesses, we all thought, would embrace broadband applications. But, those applications depend on making sure that broadband networks go right to the home and office. And, although Global Crossing serves few individual consumers, we are an important supplier of network facilities and services to other telecommunications providers and businesses who count individuals among their retail customers.

Even leaving aside the slow deployment and take up of broadband to the home, today there remain significant constraints on local access for thousands of businesses. This is particularly so for those outside the main metro areas. For new telecommunications competitors, who want to satisfy that demand, the costs of local access are still high, given the current structure of the industry.

Global Crossing and other next-generation telecommunications companies relied on forecasts of explosive demand for bandwidth, forecasts that were based on expectations of new applications and on hopes of addressing and resolving the issues of access and cost of local infrastructure. We built out our networks to meet this expected demand. Creating bandwidth, whether across oceans or land, is not instantaneous. Due to the long lead times necessary to plan, finance and construct new facilities, companies such as ours always have to build ahead of actual demand, which requires that our planning for new facilities looks ahead for several years. With actual and projected growth rates for capacity that approached 100% annually, it is clear that planning ahead for even one year implied the need to build massive amounts of capacity ahead of actual demand. For these reasons, we always have more capacity than we would need to serve our present customers. In short, at any point in time and in any one market, supply may well, and quite appropriately, exceed the existing demand.

For this reason, Global Crossing, like other large telecommunications companies, understood that, as new capacity came on-line, there might well be a temporary excess of the supply of capacity over demand in some markets and for a limited period of time. Multiple independent studies undertaken at the time, however, suggested that demand would continue to increase at very high rates and that any temporary oversupply would be extremely short-lived. The reports of experienced industry analysts indicated that any overcapacity would be swallowed up within a year or two in all geographic areas. Multiple industry experts and analysts predicted that the temporary oversupply in trans-Atlantic capacity would be consumed by 2003, and in trans-Pacific capacity by 2004. These same studies suggested that even after this supply had been exhausted, demand would continue to grow by leaps and bounds for years to come.

What happened in the middle of 2001, however, is that our customers increasingly perceived that there was an oversupply of capacity. In fact, competing systems were built, while many more were announced, but never built. Carrier and enterprise customers decided to wait out the market because they thought that if they held off on making purchases, they could negotiate a better deal from telecommunications providers. In addition, deployment of broadband across the last mile was turning out to be slower than had been forecast by industry experts. For these reasons, demand for our network and services did not increase as much as we had planned, in significant measure because our carrier customers did not continue to buy capacity to serve their retail users.

At the same time, and partly as a consequence of the perception of a supply glut, prices dropped more rapidly than had been expected in many of the major markets that we serve. Our industry had been accustomed, of course, to price declines that were driven by advances in technology that were even more rapid than those experienced in the computer industry in recent decades. In the market for broadband telecommunications capacity, the declines in prices had been more than offset by the exploding demand for more capacity, leading to growing revenues. By the end of 2001, however, while price declines had continued to exceed forecasts and expectations, the demand for capacity had slowed.

In addition to the slower-than-expected rollout of broadband applications, the broader economic crunch hit our industry, and hit it hard. The economy slowed down in the United States and worldwide, and our service revenues did not grow as rapidly as we had predicted. The capital markets, which had previously enabled, even encouraged, the existence of many emerging telecommunications and Internet companies who were large purchasers of bandwidth, closed down for these companies. Even the large incumbent telecommunications carriers, who were large customers of ours, had financial challenges of their own, whether from the economic slowdown, increased competition, the demands of improving their own networks or acquisitions of 3G wireless licenses at auction in Europe.

We were not the only telecommunications company to get caught in this "perfect storm" of slowing growth in demand, declining prices, a perceived glut and an economic and financial downturn. We had incurred over $8 billion in debt in order to construct and operate our global network and, as the year progressed, we realized that it would be increasingly difficult to meet the requirements of that debt.

Early in the fourth quarter of 2001, I was asked to serve as Global Crossing's CEO. My leadership team and I quickly undertook the further steps that were needed to streamline the company's operations. We eliminated layers of management, implemented dramatic cost reductions, including a reduction in force from nearly 14,000 to 5,000 employees, and redesigned the company's business and financial models. Despite these necessary and painful measures, it became apparent that our debt service, coupled with a realistic assessment of the market opportunities in the context of a continued slow-down in the economy, required Global Crossing to explore all its options.

Towards the end of the year, we accelerated discussions with banks and potential investors. As the pressure of loan obligations increased, however, our advisors counseled us that the Company's situation called for measures more drastic than originally expected, and, with great regret, we filed for bankruptcy protection on January 28 of this year.

We were neither the first nor the last telecommunications company to seek bankruptcy protection. As *The Wall Street Journal* reported in early 2001, telecommunications companies had borrowed more than $1.5 trillion from banks since 1996 and issued over $600 billion in bonds in order to invest in their networks. Given these debt loads, many telecommunications enterprises were forced to cut back their operations and, in the case of some, file for bankruptcy. Inevitably and unfortunately, many people who were employed by them, and many others who invested in these companies, personally experienced the ensuing turmoil.

Government Inquiries

The media continue quite naturally to highlight allegations of accounting irregularities and the role that they may have played in bringing about the current crisis. Each of us sitting at this table is reportedly the subject of government inquiries into various accounting practices. With respect to Global Crossing, the media have reported that the government is examining issues related to the accounting methods or procedures our company used for sales and purchases of capacity in the form of Indefeasible Rights of Use, or IRUs, in connection with concurrent transactions with our carrier customers.

I do not believe that the way in which Global Crossing accounted for specific transactions played any role in our financial troubles. The sale and acquisition of capacity via contracts known as IRUs is an essential part of creating efficient networks. Transactions involving IRUs are legitimate and important to both buyers and sellers of capacity and have been used for many years in the industry. Accounting for the concurrent transactions raised several very complex issues; in fact, we spent a great deal of time working with our independent auditors to determine how to account for them appropriately.

It is far too simplistic to assert that the widespread problems in the telecommunications industry were caused by particular methods of accounting. Whether other companies' difficulties are accounting-related, we cannot say. At Global Crossing, however, we know that the transactions in question represented a relatively small portion of our business, and that our accounting for them does not explain why we found it necessary to seek bankruptcy protection.

We are, of course, cooperating fully with the investigations by government bodies into our accounting practices. We have provided documents and testimony to the SEC regarding the subject transactions and precisely how we accounted for them. We have also made our employees available to be interviewed by the staff of the Energy & Commerce Committee of the House of Representatives, and in March I testified before the Subcommittee on Oversight and Investigations of the Financial Services Committee of the House of Representatives. For our own part, Global Crossing's Board of Directors has appointed a special committee of independent directors, which is conducting a review of the Company's accounting practices for the concurrent transactions.

Post-Bankruptcy Events at Global Crossing

I believe there are important lessons to be learned from our experience at Global Crossing as we look forward. Our network is still fully operational. We have thousands of dedicated and loyal employees who have maintained uninterrupted service across our network since our bankruptcy filing. We have substantially cut our capital and operating expenditures, and we have met all of our operational goals.

Delivering top quality service is still our highest goal. We continue to meet the national and worldwide needs of our tens of thousands of customers. The fact of our bankruptcy has not disrupted or affected a single customer. It is our hope that the steps we have taken will allow Global Crossing to continue to compete as an ongoing business. We are aggressively pursuing plans to emerge from Chapter 11 with our network intact.

Our financial performance since filing for Chapter 11 protection has met or exceeded our expectations. We are winning new customers and retaining our existing customers at rates higher than we had forecast. We continue to achieve an availability rate of 99.999% on our IP network, a level of performance that matches the best in the industry. Since we filed for Chapter 11 protection, our revenue, earnings, and cash have all exceeded the expectations that we established with our creditors. At the same time, our monthly operating expenses are now 40% lower than they were at the end of last year. IP traffic across our network shows healthy growth in light of the current environment.

What does the future hold for Global Crossing? It is hard to say, because we are in the middle of a complex restructuring process governed by the bankruptcy law. The future ownership of the company is being determined by the confidential auction that is now proceeding, and we expect to present the results of that auction to the Bankruptcy Court next week. Although our future is not entirely certain, we believe that we will emerge from this process with our network intact, and with new, more efficient ways of running our business.

Before I conclude, let me add some thoughts on the role of government in restoring financial health to the telecommunications sector.

Although some have argued that, in a time of turmoil, it may be appropriate for government to intervene in the market, to apply a heavier regulatory hand to the telecommunications industry, we believe that the FCC should stay on course in instituting measures that ensure fair competition and a level playing field between incumbents and new competitors. We believe the FCC, supported by the Congress, can continue to play an important role, working with industry and Wall Street, to assist the industry in transitioning out of our financial crisis.

We urge the Committee, along with the rest of Congress, the Administration and the FCC, to do what they can to open up the remaining telecommunications bottleneck in the local market, including through enforcement and monitoring of the obligations of Section 271 of the Communications Act. With respect to the local market, it is essential to do what is needed to promote competition and, most importantly, to bring down the prices of local access so that the promise of broadband can be realized. In addition, Congress has an opportunity to legislate on the issue of the fees charged for public rights of ways and for access to buildings. Adopting nondiscriminatory policies and ensuring that fees are reasonable, to allow fairer access to public rights of way, will help stimulate demand, promote consumer choice and lay the foundation for a healthier industry.

We believe that this industry will, one way or another, come through this difficult period. We cannot be sure how long the crisis will last. At Global Crossing, we started down the path of restructuring nearly a year ago. We have demonstrated that a turn-around is possible where management implements a focused and pragmatic plan, including often painful, but necessary, cost-reductions. This week, we expect that the competitive bidders who have come forward with proposals to invest in Global Crossing will make their final offers. And, early next year, we expect to emerge from the Chapter

11 process. When we do, we fully intend to continue serving our customers, just as we remain confident in our founding vision, of a global, seamless fiber-based IP network.

Mr. Chairman and members of the Committee, the current financial turmoil need not have a permanent effect on our world-leading telecommunications industry. With the cooperation of our industry partners, the financial markets, the Congress, the Administration and the FCC, we can restore the confidence of the American people and the world. During the last decade, our country has undergone a communications revolution that has produced substantial social and economic benefits. We believe that the industry will recover from its current financial crisis and that it will continue as an integral part of the engine for economic growth. On behalf of the thousands of Global Crossing employees and our customers, let me reaffirm that we very much expect to be part of that recovery and resurgence.

Thank you, once again, for inviting us to testify.