Corporate Citizenship: Helping the Communities We Serve

As a leading corporate citizen, NYNEX gives high priority to helping people communicate through technology — and helping people enrich their lives. In 1995, we distributed approximately $19.5 million in grants, matching gifts and voluntary recognition program awards. Our grant-making philosophy is guided by three priorities:

1) Improve the quality of education;
2) Promote long-term wellness by supporting health and human-services programs; and
3) Promote diversity by sponsoring cultural and community partnerships.

For information about NYNEX's philanthropic programs, or for a complete list of contributions, write to, call or fax: NYNEX, Corporate Philanthropy, 1095 Avenue of the Americas, New York, NY 10036. Phone: (800) 360-7955; Fax: (212) 398-0951.

The e-mail address for Corporate Philanthropy is notes.sdubose@a50vm1.trg.nynex.com
Information about our philanthropic programs also is featured on NYNEX's World Wide Web site (http://www.nynex.com).

1995 Financial Results

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Management's Discussion and Analysis of Financial Condition and Results of Operations

Nature of Operations

NYNEX Corporation ("NYNEX") is a global communications and media corporation that provides a full range of services in the northeastern United States and in high growth markets around the world. NYNEX has expertise in telecommunications, wireless communications, directory publishing, and video entertainment and information services. NYNEX's principal operating subsidiaries are New York Telephone Company ("New York Telephone") and New England Telephone and Telegraph Company ("New England Telephone") (collectively, the "telephone subsidiaries"). Intrastate communications services are regulated by various state public service commissions ("state commissions"), and interstate communications services are regulated by the Federal Communications Commission ("FCC").

Business Restructuring

NYNEX's 1993 results included pretax charges of $2.1 billion ($1.4 billion after-tax) for business restructuring, predominantly within the telecommunications business. Business restructuring resulted from a comprehensive analysis of operations and work processes, resulting in a strategy to redesign them to improve efficiency and customer service, to adjust quickly to accelerating change, to implement work force reductions, and to produce savings necessary for NYNEX to operate in an increasingly competitive environment.

The 1993 charges were comprised of: $1.1 billion in employee termination costs to reduce the work force by approximately 16,800 employees by the end of 1996; $626 million of process re-engineering charges, primarily for systems redesign and work center consolidation; $283 million in costs associated with planned exits from certain nontelecommunications businesses; and $106 million for asset write-offs and loss contingency accruals.

1995 and 1994 Additional Charges

During 1994, NYNEX announced retirement incentives to provide a voluntary means of implementing substantially all of the planned work force reductions. The retirement incentives were to be offered at different times through 1996 according to local force requirements and were expected to generate an estimated additional $2.0 billion in pretax charges ($1.3 billion after-tax) over that period of time as employees elected to leave the business through retirement incentives rather than through the severance provisions of the 1993 force reduction plan. In 1995 and 1994, respectively, approximately 4,700 and 7,200 employees accepted the incentive plan. This resulted in $514.1 million ($326.8 million after-tax) and $693.5 million ($452.8 million after-tax), respectively, of incremental charges for the cost of retirement incentives. The reserves established in 1993 for severance have been and will continue to be transferred primarily to the pension liability on a per employee basis as a result of employees' accepting the retirement incentives. Much of the cost of the enhancements will be funded by NYNEX's pension plans.

Employee Reductions

The 1993 employee termination costs of $1.1 billion were comprised of $586 million for employee severance payments (including salary, payroll taxes, and outplacement costs) and $520 million for post-retirement medical costs (total after-tax charges were $700 million). These costs were for planned work force reductions of 4,200 management employees and 12,600 nonmanagement employees. At December 31, 1994, the actual number of employees who elected to leave through retirement incentives in 1994 and the expectation for 1995 and 1996 were as follows:

	1994	1995	1996	Total
Management	3,700	500	—	4,200
Nonmanagement	3,500	5,600	3,500	12,600
Total	7,200	6,100	3,500	16,800

At December 31, 1994, the actual additional pretax charges for the retirement incentives and related postretirement medical costs in 1994, and the expected additional charges for 1995 and 1996 were as follows:

(In millions)	1994	1995	1996	Total
Management	$ 191	$ 31	$ —	$ 222
Nonmanagement	503	804	434	1,741
Total	$ 694	$ 835	$ 434	$ 1,963

Current Status

During 1995, it became evident that the number of management employees leaving under the retirement incentives would exceed the original estimate due to additional management staff reduction efforts. It was also determined that, due to volume of business growth, the expected reduction in the number of nonmanagement employees would be less and would not be fully realized until 1998.

The actual number of employees who elected to leave through retirement incentives in 1994 and 1995 are as follows:

	1994	1995	Total
Management	3,700	**2,300**	6,000
Nonmanagement	3,500	**2,400**	5,900
Total	7,200	**4,700**	11,900

At the present time, NYNEX expects the total number of employees who will elect to take the pension enhancements to be in the range of 17,000 to 18,000, consisting of approximately 7,000 management and 10,000 to 11,000 nonmanagement employees depending on work volumes, needs of the business, and timing of the incentive offers.

NYNEX continues to monitor the estimated additional charges to be recorded and, at December 31, 1995, still anticipates the additional charges to be in the range of $2.0 billion ($1.3 billion after-tax), despite the increase in the expected number of employees who will elect to take the incentive. This estimate is based on favorable actuarial experience for actual postretirement medical costs, and favorable demographics of employees actually accepting the offer, which have resulted in per capita charges being somewhat lower than expected. The actual additional pretax charges for the retirement incentives and related postretirement medical costs in 1994 and 1995 are as follows:

(In millions)	1994	1995	Total
Management	$ 191	**$ 268**	$ 459
Nonmanagement	503	**246**	749
Total	$ 694	**$ 514**	$ 1,208

At the present time, it is expected that the future additional pretax charges for retirement incentives will be approximately $600 to $800 million, consisting of $100 million for management and in the range of $500 to $700 million for nonmanagement employees.

The actual severance reserves utilized and the application of the postretirement medical liability established in 1993 during 1994 and 1995 are shown below:

Severance Reserve

(In millions)	1994	1995	Total#
Management*	$ 303	**$ 53**	$ 356
Nonmanagement	34	**29**	63
Total	$ 337	**$ 82**	$ 419

* 1994 includes $45 million of the 1991 severance reserves remaining at December 31, 1993.

The severance utilization amounts in 1995 and 1994 are comprised of $79 and $315 million, respectively, of severance reserves transferred to the pension liability and $3 and $22 million, respectively, utilized for other retiree costs.

Postretirement Medical Liability

(In millions)	1994	1995	Total
Management	$ 129	**$ 20**	$ 149
Nonmanagement	50	**52**	102
Total	$ 179	**$ 72**	$ 251

Assuming that employees will continue to leave under the retirement incentives, it is expected that the remaining $212 million of severance reserves will be utilized and the remaining $269 million of the postretirement medical liability will be applied in the years 1996 through 1998.

Process Re-engineering

Approximately $626 million of the 1993 charges ($395 million after-tax) consists of costs associated with re-engineering service delivery to customers. During the period 1994 through 1996, NYNEX is decentralizing the provision of residence and business customer service throughout the region, creating regional businesses to focus on unique markets, and centralizing numerous operations and support functions. At December 31, 1994, the actual 1994 utilization of reserves for process re-engineering and the revised expected utilization for 1995 and 1996 were as follows:

(In millions)	1994	1995	1996	Total
Systems redesign	$ 108	$ 162	$ 2	$ 272
Work center consolidation	27	97	49	173
Branding	21	21	—	42
Relocation	—	6	1	7
Training	—	21	28	49
Re-engineering implementation	43	28	12	83
Total	$ 199	$ 335	$ 92	$ 626

Systems redesign is the cost of developing new systems, processes and procedures to facilitate implementation of process re-engineering initiatives in order to realize operational efficiencies and enable NYNEX to reduce work force levels. These projects consist of radical changes in the applications and systems supporting business functions to be redesigned as part of the restructuring plan. All of the costs associated with these projects are incremental to ongoing operations. Specifically, only software purchases and external contractor expenses, which are normally expensed in accordance with NYNEX policy, were included in the 1993 restructuring charges. The business processes included in systems redesign are customer contact, customer provisioning, customer operations, and customer support.

Customer contact represents the direct interface with the customer to provide sales, billing inquiry and repair service scheduling on the first contact. *Customer provisioning* involves the development of the network infrastructure, circuit and dialtone provisioning and installation, and process standardization. *Customer operations* focuses on network monitoring and surveillance, trouble testing, dispatch control, and proactive repair, with reliability as a critical competitive advantage. *Customer support* facilitates low-cost, reliable service by providing support for the other three business processes.

Work center consolidation costs are incremental costs associated with establishing work teams in fewer locations to take advantage of lower force levels and system efficiencies, such as moving costs, lease termination costs (from the date premises are vacated), and other consolidation costs. *Branding* includes the costs to develop a single "NYNEX" brand identity associated with restructured business operations. *Relocation* costs are required to move personnel to different locations due to work center consolidations and include costs based on NYNEX's relocation guidelines and the provisions of collective bargaining agreements. *Training* costs are for training nonmanagement employees on newly-designed, cross-functional job positions and re-engineered systems created as part of the restructuring plan, which will permit one employee to perform tasks formerly performed by several employees, and include tuition, out-of-pocket course development and administrative costs, facilities charges, and related travel and lodging. *Re-engineering implementation* costs are incremental costs to complete re-engineering initiatives.

Current Status

At December 31, 1995, the actual 1994 and 1995 utilization of reserves and the revised expectation for 1996 are as follows:

(In millions)	1994	1995	1996	Total
Systems redesign	$ 108	**$ 207**	$ 61	$ 376
Work center consolidation	27	**51**	43	121
Branding	21	**11**	1	33
Relocation	—	**3**	2	5
Training	—	**6**	12	18
Re-engineering implementation	43	**27**	3	73
Total	$ 199	**$ 305**	$ 122	$ 626

Systems redesign: During 1994, it was determined that systems redesign would require a larger than anticipated upfront effort to fully integrate interfaces between various systems and permit development of multi-tasking capabilities. A higher degree of complexity and additional functionality required by real-time, interactive systems contributed to the increase. During 1995, systems estimates increased due to the complexity and extensiveness of integration testing and quality assurance processes. Approximately $84 and $44 million relating to software systems that were addressed by the restructure plan but not specifically provided for in the 1993 accrual was expensed in 1995 and 1994, respectively.

The actual 1994 and 1995 utilization and the revised expected utilization in 1996 of the systems redesign reserves, by business process, are as follows:

(In millions)	1994	1995	1996	Total
Customer contact	$ 52	**$ 109**	$ 30	$ 191
Customer provisioning	11	**21**	—	32
Customer operations	19	**44**	26	89
Customer support	26	**33**	5	64
Total	$ 108	**$ 207**	$ 61	$ 376

Work center consolidation was revised in 1994 for an increase in the number of work centers from what was originally planned based on union agreements. The revised estimate for 1996 is based on actual costs incurred to date and reflects the completion of the majority of the planned work centers. *Relocation* of employees was revised downward in 1994 due to the increase in the number of work centers and terms of the union agreements. At the end of 1995, the majority of the work centers are complete. *Training* was delayed in 1994 due to the timing of the union agreements and the higher degree of complexity of systems redesign; total expected costs were decreased due to the planned use of more in-house training. Training was accomplished in 1995 through in-house, on-the-job and multi-media training. *Re-engineering implementation* is winding down and will be reported with the related projects in 1996.

Other Restructuring Charges

Approximately $283 million of the 1993 restructuring charges ($271 million after-tax) related to NYNEX's sale or discontinuance of its information products and services businesses, including the sale of AGS Computers, Inc. ("AGS") and several of its business units and The BIS Group Limited ("BIS"). These charges included the write-off of the net book value of the businesses and estimated provision for future operating losses and disposal costs. NYNEX utilized $22, $62 and $185 million in 1995, 1994 and 1993, respectively, of these restructuring reserves. It is expected that the remaining balance of $14 million will be utilized in 1996.

An additional $106 million ($69 million after-tax) was recorded in 1993 for write-offs of assets and accrual of loss contingencies directly associated with restructuring at other nontelephone subsidiaries. These reserves were not utilized in 1995, but were utilized in 1994 and 1993 in the amounts of $51 (primarily for the disposition of NYNEX Properties Company) and $9 million, respectively. It is estimated that the remaining balance of $46 million will be substantially utilized in 1996.

Future Cash Effects and Cost Savings
The 1993 restructuring charges had anticipated approximately $550 million in cash outflows during the three-year period from 1994 through 1996 for severance and re-engineering costs. In 1994, NYNEX implemented retirement incentives and no longer expects to incur significant severance costs for the planned work force reductions. Cash outflows for 1993 re-engineering accruals are expected to total approximately $395 million ($125, $191, and $79 million in 1994, 1995, and 1996, respectively). Noncash restructuring charges include the pension enhancements, postretirement medical costs, charges related to discontinuance of information products and services businesses, and write-offs of assets at other nontelephone subsidiaries. Capital expenditures for 1994 through 1996 are expected to total approximately $560 million ($170, $230 and $160 million in 1994, 1995, and 1996, respectively), primarily related to systems re-engineering and work center consolidation. Over time, it is anticipated that savings generated by restructuring will provide the funds required, and any short-term cash flow needs will be met through NYNEX's usual financing channels.

Since the inception of process re-engineering and the special pension enhancement program in 1994, approximately 11,900 employees have accepted the retirement incentives. On an annualized basis, this will equate to an average reduction in wages and benefits of approximately $650 million. Partially offsetting these cost savings will be the effects of wage and price inflation, growth in volume of business and higher costs attributable to service improvements.

It is anticipated that the restructuring will result in reduced costs during the period of restructuring and reduced annual operating expenses of approximately $1.7 billion beginning in 1997. These savings include approximately $1.1 billion in reduced wage and benefit expenses due to lower work force levels, and approximately $600 million in non-wage savings including reduced rent expense for fewer work locations and lower purchasing costs. Partially offsetting these savings are higher costs due to inflation and growth in the business.

Results of Operations

NYNEX reported a net loss for the year ended December 31, 1995 of $(1.8) billion, or $(4.34) per share. Net income for the year ended December 31, 1994 was $792.6 million, or $1.89 per share. The net loss for the year ended December 31, 1993 was $(394.1) million, or $(.95) per share.

The net loss for 1995 includes an extraordinary charge and non-recurring charges and credits totaling $3.2 billion after-tax, or $7.61 per share. Included in this amount are: an extraordinary charge of $2.9 billion, or $6.84 per share, for the discontinuance of Statement of Financial Accounting Standards No. 71 ("Statement No. 71") (see Note B); charges of $549.5 million, or $1.29 per share, for non-recurring items and for pension enhancements; a gain of $155.1 million, or $.36 per share, as a result of an initial public offering ("IPO") of NYNEX's UK cable business (see Note J); and a net gain of $67.4 million, or $.16 per share, from the sale of certain cellular properties as a result of the formation of the Bell Atlantic NYNEX Mobile cellular partnership ("BANM") (see Note F). Results for 1994 include an after-tax charge of $452.8 million, or $1.08 per share, for pension enhancements. Adjusting for these items, 1995 net income was $1.4 billion, an increase of 12.1% over 1994. Results for 1993 include after-tax charges of $1.6 billion, or $3.95 per share, for business restructuring and other charges. Adjusting for these charges, 1993 net income was $1.2 billion.

Operating revenues for 1995 were $13.4 billion, an increase of $100.3 million, or .8%, over 1994. Included in this increase were changes in presentation in 1995 of gross receipts tax and revenues from NYNEX Mobile Communications Company ("NYNEX Mobile") as a result of the BANM cellular partnership (see Note A). Adjusting for these items, operating revenues increased 3.8% to $13.1 billion. Revenues from the telephone subsidiaries and Telesector Resources Group, Inc. (collectively, the "telecommunications group") increased 3.0% to $11.9 billion, and revenues from NYNEX's other subsidiaries (the "nontelephone subsidiaries") increased 11.6%, to $1.2 billion. Supporting the telecommunications group's revenue growth were a 3.4% growth in access lines and an 8.6% increase in access usage over last year.

Operating revenues for 1994 were $13.3 billion, a decrease of $101.2 million, or .8%, from 1993. Included in this decrease were changes in presentation of revenues from NYNEX Mobile and from information products and services businesses that were sold in 1993 and 1994. Adjusting for these items, operating revenues increased .4% to $12.6 billion. Revenues from the nontelephone subsidiaries increased 6.4% to $1.1 billion, supported by growth in NYNEX CableComms' customer base. Revenues from the telecommunications group were essentially flat at $11.5 billion, due principally to a revenue reduction ordered by the New York State Public Service Commission ("NYSPSC").

Operating expenses for 1995 were $11.3 billion, a decrease of $235.7 million, or 2.0%, from 1994. Included in this decrease (and as described below) were: pension enhancement charges in both periods; non-recurring net charges in 1995; and changes in presentation in 1995 of gross receipts tax and expenses from NYNEX Mobile as a result of the BANM cellular partnership (see Note A). Adjusting for these items, operating expenses were $10.3 billion, an increase of $93.8 million, or .9%. At the telecommunications group, operating expenses increased $8.1 million, or .1%, and at the nontelephone subsidiaries, operating expenses increased $85.7 million, or 9.8%.

Operating expenses for 1994 were $11.6 billion, a decrease of $1.5 billion, or 11.7%, from 1993. Included in this decrease (and as described below) were: business restructuring and other charges in 1993; pension enhancement charges in 1994; and changes in presentation of expenses from NYNEX Mobile and from information products and services businesses that were sold in 1993 and 1994. Adjusting for these items, operating expenses were $10.2 billion, an increase of $122.7 million, or 1.2%. At the telecommunications group, operating expenses increased $119.6 million, or 1.3%, and at the nontelephone subsidiaries, operating expenses were essentially flat.

Operating income, adjusting for non-recurring items and the year-over-year change in the operating income of NYNEX Mobile, was $2.8 billion in 1995, an increase of $381.9 million, or 15.9%. Operating margin for 1995 improved 2.2 percentage points to 21.3% from 19.1%. This improvement resulted from increased productivity as adjusted expense growth of .9% was outpaced by adjusted revenue growth of 3.8%.

Operating income, adjusting for non-recurring items and the year-over-year changes in the operating income of NYNEX Mobile and the information products and services businesses that were sold, was $2.4 billion in 1994, a decrease of $73.0 million, or 3.0%. Operating margin for 1994 declined to 19.1% from 19.7%, resulting from adjusted expense growth of 1.2% exceeding adjusted revenue growth of .4%.

Operating Revenues

(In millions)	1995	1994	1993
Local service	$ **6,722.2**	$ 6,605.4	$ 6,472.9
Long distance	**1,039.2**	1,081.2	1,134.4
Network access	**3,557.5**	3,447.0	3,387.2
Other	**2,088.0**	2,173.0	2,413.3
Total operating revenues	**$ 13,406.9**	$ 13,306.6	$ 13,407.8

Local service revenues increased $116.8 million, or 1.8%, in 1995 due primarily to a net $164 million increase in demand driven by growth in access lines and sales of calling features. This increase was partially offset by $35 million in rate reductions in New York and Maine, an $8 million decrease attributable to potential customer billing claims at New York Telephone, and a $5 million decrease due to the 1994 reversal of previously deferred revenues in Rhode Island.

Local service revenues increased $132.5 million, or 2.0%, in 1994 due primarily to: a net $240 million increase in demand driven by growth in access lines, sales of calling features and higher usage associated with winter storms, and a $23 million increase in rates due to a rate restructuring in Massachusetts (offset by decreases in long distance rates mentioned below), partially offset by a $135 million revenue reduction pursuant to an NYSPSC order.

Long distance revenues decreased $42.0 million, or 3.9%, in 1995 due primarily to: $24 million in required rate reductions at New England Telephone; $7 million in price reductions in New Hampshire; and a decrease in demand for wide area telecommunications services as a result of customer shifts to lower priced services offered by the telephone subsidiaries and increased competition. It should be noted that certain competitive losses in long distance revenues are mostly offset by increases in network access revenues.

Long distance revenues decreased $53.2 million, or 4.7%, in 1994 due primarily to: $25 million in rate decreases due to the previously mentioned Massachusetts rate restructuring; $8 million in price reductions in New Hampshire; a $13 million revenue reduction pursuant to an NYSPSC order; a $12 million shift in interstate toll revenues from long distance to network access at New York Telephone; and the previously mentioned decrease in demand for wide area telecommunications services. These decreases were partially offset by increased demand for message toll services.

Network access revenues increased $165.7 million, or 4.8%, in 1995 excluding a $55.2 million decrease attributable to a change in the presentation of gross receipts tax collected by New York Telephone on behalf of interexchange carriers. (In the third quarter of 1995, as a result of a change in tax law, New York Telephone was no longer required to pay gross receipts tax to New York State on interstate access revenues. Prior to this change, these taxes were collected from interexchange carriers and remitted to the taxing authority and were included in both operating revenues and operating expenses) (see *Operating expenses*.) The increase in Network access revenues resulted from a $157 million increase in interstate demand partially offset by a $29 million reduction in interstate rates, and a $44 million increase in intrastate demand partially offset by a $10 million reduction in intrastate rates.

Network access revenues increased $59.8 million, or 1.8%, in 1994. There was a $127 million increase in interstate demand partially offset by a $69 million reduction in interstate rates, and a $21 million increase in intrastate demand offset by a $24 million reduction in intrastate rates. In addition, there was a $12 million increase at New York Telephone due to the aforementioned shift in interstate toll revenues and a $12 million recognition of previously deferred revenues, partially offset by a $12 million revenue reduction pursuant to an NYSPSC order.

Other revenues increased $235.2 million, or 16.2%, in 1995, after adjusting for a $320.2 million decrease associated with the July 1, 1995 deconsolidation of NYNEX Mobile due to the formation of the BANM cellular partnership (see Note A) ($399.8 million for six months of 1995 compared with $720.0 million for twelve months of 1994). The increase of $235.2 million reflects the following: NYNEX CableComms revenues increased $70.2 million, more than doubling, due to significant increases in cable television customers and in residence and business telecommunication lines. NYNEX Information Resources revenues increased $48.7 million, or 5.4%, due primarily to increased Yellow Pages advertising revenues, from both domestic and international directories. Telecommunications revenues increased $110.2 million, due to the following at New York Telephone: (1) $109.2 million due to the cessation of "setting aside" revenues in the second quarter of 1995 as a result of an NYSPSC order approving a performance-based regulatory plan (the "Plan"), (2) $10 million due to the elimination of the deferral of intrastate revenues as a result of the discontinuance of regulatory accounting principles (see Note B), (3) $4.5 million from revenues earned under a service improvement plan implemented in 1994 and (4) $5 million recognized in connection with intraLATA presubscription ("ILP") commitments that were met in 1995. These increases were partially offset by a $22 million decrease in billing and collection revenues pursuant to a contract with AT&T Corp.

With respect to (1) above, future quarters will no longer reflect the setting aside of revenues of $38 million per quarter experienced in 1994 and early 1995. At December 31, 1995, $188 million of revenues remains deferred ($161 million pursuant to the Plan and $27 million pursuant to the service improvement plan) and will be recognized as commitments are met or obligations are satisfied (see **State Regulatory**).

Other revenues decreased $89.4 million, or 5.8%, in 1994, after adjusting for a $279.5 million increase associated with the deconsolidation of NYNEX Mobile ($720.0 million for 1994 compared with $440.5 million for 1993) and a $430.4 million decrease associated with the sale of information products and services businesses. The decrease of $89.4 million reflects the following: Telecommunications revenues decreased $153.8 million, due principally to a $153 million revenue reduction ordered by the NYSPSC. NYNEX Information Resources revenues increased $22.2 million, or 2.5%, reflecting higher Yellow Pages advertising revenues and increased revenues from the publication of directories in the Czech Republic. NYNEX CableComms revenues increased $37.0 million, more than doubling in 1994.

Operating Expenses

(In millions)	1995	1994	1993
	$ 11,314.7	$ 11,550.4	$ 13,074.5

Operating expenses for 1995 were $11.3 billion, a decrease of $235.7 million, or 2.0%, from 1994. Included in this decrease (as discussed below) were: pension enhancement charges in both periods; nonrecurring net charges in 1995; and changes in presentation in 1995 of gross receipts tax and expenses from NYNEX Mobile as a result of the BANM cellular partnership. Adjusting for these items, operating expenses were $10.3 billion, an increase of $93.8 million, or .9%.

Operating expenses for 1994 were $11.6 billion, a decrease of $1.5 billion from 1993. Included in this decrease (as discussed below) were: business restructuring and other charges in 1993; pension enhancement charges in 1994; and changes in presentation of expenses from NYNEX Mobile and from information products and services businesses that were sold. Adjusting for these items, operating expenses were $10.2 billion, an increase of $122.7 million, or 1.2%.

Operating expenses included pretax pension enhancement charges of $514.1 million and $693.5 million in 1995 and 1994, respectively. The non-recurring net charges in 1995 included: (1) accruals of $291.5 million related to various self-insurance programs, legal and regulatory contingencies, operating tax provisions and revised benefit charges, reflecting events that occurred in 1995 and additional information made available through revised estimates and analyses completed during 1995, and (2) a $53.5 million net expense reduction resulting primarily from the recognition of a pension curtailment gain and certain non-recurring charges associated with the formation of the BANM cellular partnership (see Note F). There was a $55.2 million change in presentation in 1995 of gross receipts tax collected by New York Telephone on behalf of interexchange carriers (see *Network access* revenues), and a $332.9 million decrease associated with the deconsolidation of NYNEX Mobile as a result of the BANM cellular partnership (see Note A) ($336.2 million for six months of 1995 compared with $669.1 million for twelve months of 1994).

At the telecommunications group, operating expenses were $9.3 billion in 1995, an increase of $8.1 million, or .1%. Employee related costs increased $9.5 million in 1995. Higher salaries and wages resulting primarily from wage rate and volume-related increases were substantially offset by reductions in the work force and lower benefit costs (including revised estimates associated with workers compensation accruals). Offsetting these increases was a $1.4 million net decrease in non-employee costs, primarily as a result of decreases in depreciation and amortization (see Note B) offset by increases in bad debt expense, advertising and marketing costs, and gross receipts taxes (primarily from a tax settlement at New York Telephone).

At the nontelephone subsidiaries, operating expenses were $959.9 million in 1995, an increase of $85.7 million, or 9.8%. This increase was almost entirely due to the expansion of NYNEX CableComms.

Operating expenses for 1994 included pretax pension enhancement charges of $693.5 million. Operating expenses for 1993 included business restructuring and other charges of $2.2 billion. There was a $290.5 million increase associated with the deconsolidation of NYNEX Mobile ($669.1 million for 1994 compared with $378.6 million for 1993) and a $435.1 million decrease associated with the sale of information products and services businesses.

At the telecommunications group, operating expenses were $9.3 billion in 1994, an increase of $119.6 million, or 1.3%. Employee related costs increased $38.0 million in 1994. Higher salaries and wages resulting from wage rate increases, single enterprise employee transfers, and volume-related increases were partially offset by reductions in the work force and lower benefit costs. In addition, there was an $81.6 million increase in non-employee costs, primarily as a result of increases in depreciation and amortization, bad debt expense, and contracted services, partially offset by decreases in property taxes.

Gain on sale of stock by subsidiary

An IPO of the shares of NYNEX CableComms Group PLC ("UK CableComms") and NYNEX CableComms Group Inc. ("US CableComms") (collectively, "CableComms") was completed in June 1995. The offering represented 33% of the total units outstanding, with NYNEX retaining the balance. Net proceeds from the offering were approximately $610 million. NYNEX recognized a pretax gain of $264.1 million in recognition of the net increase in the value of NYNEX's investment in CableComms (see Note J).

Other income (expense) - net

(In millions)	**1995**	1994	1993
	$ (4.9)	$ (43.8)	$ (97.0)

Other income (expense) - net for 1995 improved $38.9 million over 1994. The principal components of this change were a $70.3 million non-recurring gain on the sale of cellular properties in connection with the formation of the BANM cellular partnership (see Note F), partially offset by a $26.7 million increase in minority interest expense and $17.4 million from unrealized "mark to market" valuation adjustments (see **Financial Instruments**).

Other income (expense) - net for 1994 improved $53.2 million over 1993. The principal components of this change were: in 1993, $84 million was expensed for the interstate portion of call premiums and other charges associated with the refinancing of long-term debt, partially offset by an $11 million increase in minority interest expense in 1994.

Interest expense

(In millions)	1995	1994	1993
	$ 733.9	$ 673.8	$ 659.5

Interest expense for 1995 increased $60.1 million, or 8.9%, over 1994 due primarily to higher average interest rates of 7.2% compared to 6.5% in 1994. The higher average interest rates are due to increased short-term rates and a lengthening in the maturity of the debt portfolio in the latter half of 1994 (77% long-term in 1995 compared to 70% in 1994). Total debt remained essentially flat at $9.8 billion. This increase in interest expense was partially offset by a reversal in 1995 of $14 million of previously recorded interest on the revenue set aside as ordered by the NYSPSC (see **State Regulatory**).

Interest expense for 1994 increased $14.3 million, or 2.2%, over 1993 due primarily to an increase in average debt levels from $8.7 billion in 1993 to $9.7 billion. However, total debt decreased $214.6 million to $9.9 billion (see **Cash Flows from Financing Activities**). Average interest rates declined from 7.3% in 1993 to 6.5% primarily as a result of long-term debt refinancings throughout 1993.

Income (loss) from long-term investments

(In millions)	1995	1994	1993
	$ 92.9	$ 57.7	$ (21.9)

Income (loss) from long-term investments for 1995 improved $35.2 million, or 61.0%, over 1994. This increase was due primarily to equity income of $90.7 million from the BANM cellular partnership (see Note F), partially offset by losses from investments in the Tele-TV Partnerships, FLAG Limited ("FLAG") and PCS Primeco.

Income (loss) from long-term investments for 1994 improved $79.6 million over 1993, principally as a result of $53 million of dividends received in 1994 from Viacom Inc. ("Viacom") and the $31 million effect of restructuring charges on 1993 amounts.

Income taxes

(In millions)	1995	1994	1993
	$ 640.9	$ 303.7	$ (172.7)

Income taxes for 1995 increased $337.2 million over 1994, attributable primarily to an increase in pretax income of $614.1 million, or 56.0%, and a five percentage point increase in the effective tax rate for 1995 primarily reflecting the discontinued application of Statement No. 71 and a $71.7 million deferred tax valuation allowance benefit in 1994.

Income taxes for 1994 increased $476.4 million over 1993, attributable primarily to an increase in pretax income of $1.5 billion in 1994 and a reduction in the effective tax rate for 1994 reflecting a $71.7 million reduction in the deferred tax valuation allowance.

Extraordinary item

The discontinued application of Statement No. 71 required NYNEX, for financial accounting purposes, to adjust the carrying amount of telephone plant and equipment and to eliminate non-plant regulatory assets and liabilities from the balance sheet. This change resulted in an after-tax charge of $2.9 billion, consisting of $2.2 billion to adjust telephone plant and equipment and $0.7 billion to write off non-plant regulatory assets and liabilities. NYNEX now utilizes shorter asset lives for certain categories of telephone plant and equipment than those previously approved by regulators. The elimination of the amortization of net regulatory assets and the effects of certain changes in accounting policies are not expected to have a significant impact on financial results in future periods (see Note B).

Capital Resources and Liquidity

Management believes that NYNEX has adequate internal and external resources available to finance ongoing operating requirements, business development, network expansion, and new investments for the foreseeable future.

During 1995, net cash used in investing activities exceeded net cash provided by operating activities by $218.1 million. This difference was funded primarily by IPO and minority interest proceeds and equity issuances.

Cash Flows from Operating Activities

Net cash provided by operating activities was $3.6, $3.7 and $3.7 billion in 1995, 1994 and 1993, respectively. In 1995, cash provided by operating activities decreased $51.9 million. Net income excluding the extraordinary item and gain on an IPO of shares of CableComms was essentially flat. Depreciation and amortization expense decreased $73.8 million, primarily at the telecommunications group as discussed above. Changes in operating assets and liabilities provided $20.9 million of cash flows in 1995 over 1994, primarily as a result of increased trade payables partially offset by increased accounts receivable. Costs associated with re-engineering activities reserved for in 1993 resulted in cash outlays of $191 million in 1995 and $125 million in 1994. Pension enhancement charges in 1995 and 1994 did not materially affect operating cash flows when recorded since the cash outflows will be incurred primarily by the NYNEX Pension Plans in future years.

In 1994, cash provided by operating activities increased $49.5 million. Net income decreased $442.5 million from 1993, after excluding $1.6 billion due to 1993 business restructuring and other charges. Depreciation and amortization expense increased $106.6 million, primarily at the telecommunications group as discussed above. Changes in operating assets and liabilities provided $203.4 million of cash flows in 1994 over 1993, primarily as a result of decreased accounts receivable and prepaid expenses, partially offset by decreased trade payables.

Excluding the effects of restructuring charges, Management anticipates cash provided by operating activities in 1996 to increase, primarily as a result of earnings growth.

Cash Flows from Investing Activities

Net cash used in investing activities was $3.9, $3.2 and $4.3 billion in 1995, 1994 and 1993, respectively.

Capital expenditures in 1995 were $3.2 billion, an increase of $175.9 million over 1994. Rapid buildout of the cable television/telecommunications network in the United Kingdom continued. The largest component of capital expenditures continues to be for the telephone subsidiaries. These capital expenditures continued at the same level over the three-year period, funded primarily through cash generated from operations, and it is anticipated that 1996 capital expenditures will be similarly funded. Total capital expenditures in 1996 are projected to remain at a level comparable to 1995.

Capital expenditures in 1994 were $3.0 billion, an increase of $295.0 million over 1993 for the construction and upgrade of mobile cell sites and the continued buildout of the cable television/telecommunications network in the United Kingdom.

Investment in leased assets: In 1995, the $71.6 million increase in investments in leased assets was the result of increased activity in the middle market portfolios at NYNEX Credit Company ("Credit Company").

In 1994, decreased investments in leased assets were the result of heightened competition in the leasing market.

Other investing activities: In 1995, cash flows from other investing activities - net were $518.3 million, $474.7 million higher than in 1994 as a result of investments in: PCS Primeco (a venture to provide national wireless communications services), BANX Partnership (a partnership formed to invest in wireless cable systems), Bayan Telecommunications Holdings Corporation, the Tele-TV Partnerships, FLAG and P.T. Excelcomindo Pratama and from the effect of cash received in 1994 from the exit from the information products and services business, partially offset by $90 million of cash received from the sale of cellular properties overlapping with Bell Atlantic Corporation's cellular properties prior to the formation of BANM.

In 1994, cash flows from other investing activities - net were $43.6 million, $1.3 billion lower than in 1993. NYNEX did not make any significant long-term investments in 1994. In 1993, cash outflows resulted from a $1.2 billion investment in Viacom and investments in: Orient Telecom & Technology Holdings Ltd. (to develop telecommunications opportunities in China), STET Hellas (a Greek cellular project) and an additional investment in TelecomAsia Corporation Public Company Limited (for a network expansion project in Thailand).

Cash Flows from Financing Activities

Short-term and long-term debt: Total debt was essentially flat in 1995 as compared to 1994. The debt ratio increased to 61.8% as of December 31, 1995, compared with 52.9% as of December 31, 1994, primarily as a result of the $2.9 billion after-tax extraordinary charge which reduced equity.

During 1995, commercial paper decreased as a result of using the proceeds from the monetization of a portion of NYNEX's investment in Viacom Preferred Stock (see *Viacom* below). Credit Company issued $135 million of medium-term notes.

During 1994, commercial paper and short-term debt decreased a net $1.7 billion, due primarily to the repayment of commercial paper through the issuance of long-term debt. New York Telephone issued $450 million in debentures and $150 million in notes and used the proceeds to repay short-term borrowings from NYNEX. The proceeds were, in turn, used by NYNEX to repay commercial paper borrowings. NYNEX Capital Funding Company ("CFC") issued $863 million of medium-term notes in order to reduce NYNEX's commercial paper requirements. It is estimated that these refinancings will continue to result in an annual interest savings of approximately $62 million for the next two years, with savings thereafter varying as debt matures.

Total debt decreased $214.6 million in 1994 as compared to 1993. The debt ratio decreased to 52.9% as of December 31, 1994, compared with 53.9% as of December 31, 1993, primarily as a result of the $1.6 billion after-tax business restructuring and other charges which reduced equity.

The majority of the telephone subsidiaries' refinancing charges in 1993, including call premiums, were deferred and amortized for intrastate rate-making purposes and were subsequently eliminated as a result of the discontinuance of Statement No. 71.

Issuance of common stock: In 1995, 1994 and 1993, NYNEX continued to issue common stock for employee savings plans, the Dividend Reinvestment and Stock Purchase Plan ("DRISPP"), stock compensation plans, and employee stock option plans. These issuances increased equity by approximately $333 million in 1995, $320 million in 1994, and $128 million in 1993. The noncash issuance of stock, primarily for dividends in connection with DRISPP, is $110, $107, and $30 million, respectively. The dividends for common stock remained unchanged at $2.36 per share in 1995, 1994 and 1993.

Purchase of treasury stock: In October 1994, NYNEX granted additional stock options in connection with the employee stock option plans established in 1992. NYNEX purchased treasury stock in 1993 and released shares into the open market as stock options were exercised. In November 1995, NYNEX began issuing new shares of its common stock as stock options were exercised.

Minority interest: Financing cash flows in 1995 included net funds of $289.2 million primarily provided by a minority interest in the financing structures formed in December 1993 and 1994 for the network construction program in the United Kingdom and by the monetization proceeds (see *Viacom* below). Financing cash flows in 1994 included net funds of $359.2 million primarily provided by a minority interest in the financing structures formed in the United Kingdom.

Proceeds from the sale of stock by subsidiary-net: During the second quarter of 1995, $610 million of proceeds were received from the IPO of CableComms (see below).

Current and Future Financing Strategies

CableComms: NYNEX CableComms is constructing and operating a $3 billion broadband (high capacity) network, to be substantially completed by 1997, for the provision of cable television and telecommunications services in certain licensed areas in the United Kingdom.

During 1993 (for licensed areas in the Southern United Kingdom or "South") and 1994 (for licensed areas in the Northern United Kingdom or "North"), NYNEX entered into a series of financing transactions that coupled a financing partnership and limited liability companies for funding construction of up to $425 million in the South and up to $1.1 billion in the North, for a total of up to $1.5 billion (as these loans are denominated in pounds sterling, these amounts are based on applicable year-end exchange rates). In connection with the financing of the South and North, NYNEX has provided certain guarantees and indemnifications to the financing partnership and limited liability companies regarding the completion of the construction program and any breach of the agreements due to events prior to the creation of the entities. This type of financing could provide significant additional funds over the first five years of each financing to help complete the funding of NYNEX CableComms' network. Management anticipates having sufficient funds, either from these or other funding sources, to complete construction of the network.

During February 1995, two entities were formed: a UK public limited liability company (UK CableComms) and a Delaware corporation (US CableComms). The sole assets of UK CableComms and US CableComms are 90% and 10%, respectively, of the outstanding stock of NYNEX CableComms Holdings, Inc. which holds, through various subsidiaries and partnerships, interests in cable television and telecommunications franchises, assets and operations in the United Kingdom.

An IPO was completed in June 1995 of 305 million equity units of CableComms. These units are traded as "stapled units" and are comprised of one ordinary share of UK CableComms and one share of common stock of US CableComms (the "Combined Offering"). The Combined Offering represented 33% of the total units outstanding, with NYNEX retaining the balance. Net proceeds from the offering were approximately $610 million. CableComms is using the proceeds to repay outstanding revolving loans under credit facilities, to fund a portion of the cost of construction of its network, and for operating cash flow and interest.

Viacom: In December 1995, NYNEX entered into a contract for the non-recourse securitization that permits a monetization of approximately 50% of its investment in the Viacom Series B Cumulative Preferred Stock, of which 8% was implemented in 1995. NYNEX realized proceeds of $100 million from this monetization which were used to reduce outstanding commercial paper.

The term of the monetization transaction is five years at which time the third party interest that provided the funding for this transaction will be redeemed through the sale of the assets securitizing this transaction. Under the terms of an extension agreement, NYNEX has the ability and intends to increase the amount of monetization up to $600 million by March 31, 1996 under terms and conditions that are substantially the same as the December 1995 transaction. NYNEX may, upon meeting certain funding requirements, elect to purchase the third party interests or terminate the transaction and cause the liquidation of the securitized assets.

At December 31, 1995, NYNEX had $950 million of unissued, unsecured debt and equity securities registered with the Securities and Exchange Commission (the "SEC"). The proceeds from the sale of these securities would be used to provide funds to NYNEX and/or NYNEX's nontelephone subsidiaries for their respective general corporate purposes. At December 31, 1995, CFC had $637 million of unissued medium-term debt securities registered with the SEC. When issued, these securities will be guaranteed by NYNEX. The proceeds from the sale of these securities may be used to provide financing for NYNEX and the nontelephone subsidiaries. At December 31, 1995, New England Telephone and New York Telephone had $500 and $250 million, respectively, of unissued, unsecured debt securities registered with the SEC.

In the third quarter of 1995, an independent bond rating agency lowered its rating of the long-term debt of NYNEX Corporation, which includes Credit Company and CFC. The bond ratings of New York Telephone and New England Telephone were reaffirmed at current levels, but the rating outlook on New England Telephone was placed on negative outlook by the agency. However, Management believes that the bond ratings are indicative of strong credit support for timely principal and interest payments in the foreseeable future.

On November 10, 1995 NYNEX and Credit Company entered into a $2.75 billion unsecured revolving credit facility, with Chemical Bank as the administrative agent. (Credit Company may borrow up to $300 million under this facility.) Further, NYNEX may request an increase in the aggregate commitments under the facility of up to $500 million. The initial term is for five years, but the borrowers may request two extensions of the facility, in each case for an additional year. Currently, a fee of .075% per annum is paid by NYNEX on the aggregate outstanding commitments. Under the terms of the agreement, the proceeds may be used to fund working capital and/or any lawful corporate purposes, including support of outstanding commercial paper. NYNEX had no borrowings under this credit facility at December 31, 1995. However, $1.9 billion of outstanding commercial paper borrowings was classified as Long-term debt at December 31, 1995 because NYNEX has the intent to refinance the commercial paper borrowings on a long-term basis and has the ability to do so under the credit facility.

The venture between NYNEX, Bell Atlantic Corporation, AirTouch Communications Inc. and U S WEST Inc. is comprised of two partnerships, one of which, PCS Primeco, participated in the FCC auction of personal communications services ("PCS") licenses and bid a total of approximately $1.1 billion for licenses in eleven cities, of which NYNEX's portion was approximately $277 million. The bid was paid upon grant of the licenses and final review of bidder qualifications by the FCC in June of 1995. NYNEX's portion of the bid was funded through the issuance of commercial paper. In 1996, the venture plans to continue to build markets and build out the network for prospective offering of services to customers.

Financial Instruments

Financial Risk Management

NYNEX has entered into transactions involving the use of derivative instruments as part of its financial risk management program. The purpose of this program is to manage NYNEX's aggregate financial risk and to protect against adverse changes in foreign exchange rates, interest rates, and other prices or rates, and to otherwise facilitate NYNEX's financing strategy, without holding or issuing any financial instruments solely for trading purposes.

The derivative instruments used to manage these risks may be separated into three fundamental types: forwards, options and swaps. NYNEX assesses financial exposures and matches its derivative positions accordingly. Liquidity and results of operations are not expected to be, but may be, materially affected by NYNEX's financing strategy, a portion of which is accomplished through the aforementioned risk management program.

NYNEX's use of derivatives for risk management purposes is represented by notional amounts. These notional values solely represent contractual amounts that serve as the basis or reference amount upon which contractually stipulated calculations are based. Therefore, these amounts are intended to serve as general volume indicators only and are not indicative of the potential gain or loss from market or credit risks, or future cash requirements. At December 31, 1995 and 1994, NYNEX had derivative transactions maturing between 1995 and 2004 with notional amounts as follows (categorized by the type of risk being managed):

(In millions)	1995	1994
Basis swaps/Swaptions	**$ 1,001.0**	$ 1,001.0
Foreign currency/Interest rate swaps	**928.4**	928.4
Foreign currency forwards (short dated)	**556.3**	—
Interest rate swaps/Caps	**279.2**	285.9
Foreign currency swaps/Other	**60.0**	61.5
Structured note swaps	**55.0**	55.0
Total	**$ 2,879.9**	$ 2,331.8

Basis swaps: In 1993, NYNEX entered into J.J.Kenny/LIBOR basis swaption agreements as part of a risk management program to protect against the effect of increased corporate tax rates on Credit Company's leveraged lease portfolio. NYNEX received approximately $12 million of premiums on the basis swaption agreements, which were exercised in January of 1994. The recording of these basis swaps at fair market value as of December 31, 1995 resulted in an unrealized mark to market adjustment of approximately $17.4 million net of previously unamortized premium, which is included in Other income (expense) - net in the consolidated financial statements.

Foreign Exchange Risk and Interest Rate Risk Management

Foreign currency/Interest rate swaps: NYNEX hedges the US Dollar value of many of its international investments. In some cases, direct borrowings in the foreign currency are used. In other cases, NYNEX uses derivatives to create synthetic non-US Dollar denominated debt, thereby hedging or funding these investments more cost-effectively and with greater flexibility. Generally these transactions involve a derivative contract which includes both interest rate and foreign currency components. With respect to the foreign currency components, cumulative net gains of $7.4 and $5.9 million at December 31, 1995 and 1994, respectively, have been recorded as direct adjustments to Stockholders' equity. In connection with managing the cost associated with the currency components, the interest rate swap components generally require NYNEX to receive interest at a fixed rate averaging approximately 3.4% and 3.3% as of December 31, 1995 and 1994, respectively, and to pay a floating interest rate (three-month or six-month LIBOR) which averaged approximately 6.1% and 6.0% on December 31, 1995 and 1994, respectively.

Foreign currency forwards (short dated): In connection with the receipt in 1995 of demand loans denominated in UK pounds from NYNEX CableComms, NYNEX entered into foreign currency forward contracts to manage the foreign currency exposures associated with the loans' repayments.

Interest rate swaps/Caps: In order to manage interest rate exposures, NYNEX employs various strategies primarily involving interest rate swaps which sometimes incorporate interest rate options. The net costs of these options are amortized to interest expense over the lives of the applicable agreements.

NYNEX has entered into several interest rate swap agreements to modify the interest rate profile of its liability portfolio. These swaps are associated with either a portion of commercial paper or non-callable medium-term notes and are designed to achieve a targeted mix of floating and fixed rate debt for the NYNEX portfolio. The following table indicates the types of interest rate swaps used for this purpose and their weighted average interest rates. Variable rates are based on the expected future rates based on the yield curve at the reporting date; those may change significantly but are not expected to have a material effect on future cash flows. These swap contracts, with remaining maturities of between one and eight years, are as follows:

(In millions)	1995	1994
Receive-fixed swaps-notional amount	**$ 186.7**	$ 186.7
Average receive rate	**6.60%**	6.60%
Average pay rate	**5.48%**	8.20%
Pay-fixed swaps-notional amount	**$ 92.5**	$ 89.2
Average pay rate	**6.08%**	6.34%
Average receive rate	**5.23%**	8.45%

Foreign currency swaps/Other: In order to mitigate the impacts of foreign currency and interest rate fluctuations on certain payments in conjunction with the financing of the network construction project in the UK, NYNEX entered into two cross-currency swaps. The contract terms for these swap agreements include foreign currency and interest rate components which are settled quarterly when payments are made and received. For the swap relating to the financing of the franchises in the North (entered into on December 19, 1994), the exchange rate is 1.5625 $/£. For the swap relating to the financing of the franchises in the South (entered into on December 31, 1993), the exchange rate is 1.4795 $/£. The swaps require NYNEX to pay in US dollars an average fixed interest rate of 13% and 15.4% for the North and South financings, respectively, and to receive a variable interest rate based on 3-Month LIBOR, payable in UK Pounds. The net impact of activities related to the swaps is recorded in income from continuing operations.

Structured note swaps: During 1994, NYNEX entered into three derivative contracts in connection with the issuance of three structured medium-term notes with a total principal amount of $55 million in order to lower financing costs. The three derivative contracts have effectively converted the structured notes into standard medium-term notes with effective interest rates of 7.18% ($20 million principal), 7.785% ($10 million principal) and 3-Month LIBOR + 0.15% ($25 million principal).

Impact on Operations

In 1995, 1994, and 1993, NYNEX's income from continuing operations was reduced by $32.0, $8.6 and $10.7 million, respectively, from all risk management activities. The $32.0 million reduction in 1995 was primarily due to $17.4 million from an unrealized "mark to market" valuation adjustment for the basis swaps. The remaining $14.6 million reduction in 1995 and reductions in 1994 and 1993 were primarily due to the interest expense associated with interest rate management and synthetic non-Dollar debt.

NYNEX's policy requires the evaluation of the hedging of international equity investments on a case-by-case basis. By hedging the foreign currency risk associated with some of these investments, NYNEX has incurred additional costs. These incremental costs reflect the higher cost of capital in the relevant international markets. For the hedges utilizing derivatives, these incremental costs have been reflected in interest expense and in the fair value of the respective derivative liabilities. As of December 31, 1995 and 1994, approximately $(34.9) and $(43.6) million, respectively, of the fair market value of derivative (hedging) liabilities reflects any remaining unamortized incremental cost of hedging equity investments in the UK and Thailand. These remaining incremental costs are discounted based upon the rates implied in the yield curve at the reporting dates. The interest expense associated with these hedges is managed as part of NYNEX's overall interest rate structure.

Collective Bargaining Agreements

In May 1994, agreements were ratified with the Communications Workers of America and the International Brotherhood of Electrical Workers ("IBEW") in New York to extend the collective bargaining agreements through August 8, 1998. A similar agreement was reached with and ratified by the IBEW in New England in August 1994. There will be basic wage increases of 10.5% during the life of the agreements. The wage rates increased 4.0% in August 1995, and will increase 3.5% and 3.0% in August 1996 and 1997, respectively. In 1997, there may also be a cost-of-living adjustment. The agreements also provide for retirement incentives, a commitment to no layoffs or loss of wages as a result of company-initiated "process change," an enhanced educational program and stock grant and other incentives to improve service quality.

Competitive and Regulatory Environment

Competition

NYNEX believes that, while it will face significantly increased risks in its traditional markets, there will be significant opportunities in its many new markets.

Federal and state regulators continue to adopt policies favoring competition and have initiated various proceedings to further those policies. Those policies will be advanced by the enactment of the Telecommunications Act of 1996, which immediately opens NYNEX's local telecommunications markets to full competition. An increasing number of national and global companies with substantial capital and marketing resources are expected to enter many of NYNEX's local markets. At the same time, the 1996 Act frees NYNEX to enter the long distance, video entertainment and information markets. NYNEX is granted immediate relief for long distance calling (both U.S. and international) originating outside of the NYNEX region, as well as for long distance services incidental to wireless, video and information services, and for video programming.

Most of the services that NYNEX provides in its local telecommunications markets have been facing increasing competition for the past several years. NYNEX has responded by obtaining increased pricing flexibility under incentive regulation, introducing new services, and improving service quality. Increases in 1995 Private Line/Special Access revenues, and the number of Centrex "win-backs" from PBX vendors indicate NYNEX's ability to respond effectively in its most competitive markets.

Competition for intraLATA toll revenues has intensified, beginning in 1994 with the increased marketing of "dial-around" programs by interexchange carriers. However, to date, the "retail" toll revenues NYNEX has lost to such programs are being offset in part by increased revenues from wholesale access charges. ILP began in New York in late 1995 and was completed in February 1996. Future wholesale pricing is the subject of pending regulatory proceedings.

In the highly competitive interstate access market, NYNEX received a waiver from the FCC in 1995, to de-average switched access rates in the metropolitan New York LATA and introduce a new fixed monthly charge paid directly by interexchange carriers. This has enabled NYNEX to charge prices that more accurately reflect the market conditions in its most competitive area.

To provide interLATA long distance service for calls originating within its region, NYNEX must meet certain technical and regulatory requirements and the FCC must determine it to be in the public interest.

NYNEX considers itself well positioned to enter the in-region long distance business quickly, as in New York and Massachusetts it already meets many of the requirements of this competitive "checklist." NYNEX provides for physical collocation of competitors' facilities and has signed interconnection agreements which include number portability and reciprocal compensation for terminating traffic with local exchange competitors. NYNEX has also unbundled many components of its network and offers them on a wholesale basis, and completed ILP in New York in February 1996.

Significant regulatory developments of 1995 are discussed below.

State Regulatory

During 1995 the telephone subsidiaries were able to replace rate of return regulation with price regulation plans in New York, Massachusetts and Maine, which represent approximately 95% of their access lines collectively. These state regulatory plans eliminate the telephone subsidiaries' obligation to share earnings with customers, allow the companies greater flexibility to vary prices to meet competition and impose service quality performance measurements. In January 1996, New England Telephone filed a proposed price regulation plan with the Rhode Island Public Utilities Commission.

Massachusetts

Incentive Plan: In Massachusetts, the price regulation plan approved by the Massachusetts Department of Public Utilities ("MDPU") governs New England Telephone's Massachusetts intrastate operations through August 2001. Certain residence exchange rates are capped, and pricing rules limit New England Telephone's ability to increase prices for most services. The MDPU also established a quality of service index and ordered that New England Telephone's inability to meet the performance levels in any given month would result in a one-twelfth of one percent increase in the productivity offset used in the annual price cap filing. New England Telephone's initial price plan tariff filing, which became effective in September 1995, contains rate changes that will result in an annual revenue reduction of approximately $38 million. The MDPU's Order has been appealed to the Supreme Judicial Court of Massachusetts.

Competition Proceeding: In 1995, hearings commenced in the MDPU's investigation of intraLATA and local exchange competition in Massachusetts. The MDPU has indicated that among the matters it intends to address are collocation, interconnection of networks, intraLATA toll presubscription, telephone number assignment and portability and universal service funding.

New York

Incentive Plan: In 1995, the NYSPSC approved with modifications a Plan that changes the manner in which New York Telephone will be regulated by the NYSPSC over the next five to seven years. Prices are capped at current rates for "basic" services such as residence and business exchange access, residence and business local calling and LifeLine service, and price reduction commitments are established for a number of services, including toll and intraLATA carrier access services. Certain prices may be adjusted annually based on an inflation index and costs associated with NYSPSC mandates and other defined "exogenous" events. Depending on whether the Plan remains in effect for five or seven years, New York Telephone's prices will have been decreased by an amount that, based on current volumes of business, would produce an aggregate revenue reduction over the term of the plan of $1.1 billion at the end of five years, or $1.9 billion at the end of seven years.

The Plan also establishes service quality targets with stringent rebate provisions if New York Telephone is unable to meet some or all of the targets, and sets an accelerated schedule for the provision of ILP. New York Telephone's compliance tariffs under the Plan became effective on a temporary basis as of September 1, 1995, and will remain temporary pending the NYSPSC Staff's review and investigation.

The NYSPSC has rejected various petitions that had been filed for reconsideration of the order approving the Plan and indicated that it had approved a Staff plan for monitoring New York Telephone's compliance. In late 1995, MCI Communications Corporation ("MCI") commenced a proceeding in the New York Supreme Court seeking to overturn the NYSPSC's orders with respect to the Plan. MCI challenges the lack of an earnings cap and asserts that New York Telephone's rates should be further reduced annually by the amount of the $153 million set-aside.

Competition II Proceeding: In 1995, the NYSPSC issued an order resolving certain issues in its proceeding on local exchange competition in New York State. New York Telephone must provide White Pages directory listings at no charge to customers of competitive local exchange carriers ("CLECs"), but may negotiate fees with CLECs for delivery of the directories to their customers. The NYSPSC also established a reciprocal compensation scheme for the payment of access rates when New York Telephone and CLECs terminate traffic on each other's networks. In general, the NYSPSC's plan permits "full-service, facilities-based" local exchange carriers to pay a lower rate than other carriers will be required to pay. The NYSPSC also determined that New York Telephone must, upon request, provide services to interconnect CLECs that are collocated in New York Telephone's central offices.

The NYSPSC also directed New York Telephone to file tariffs to remove restrictions on the resale of residential services, effective February 1996, or to show cause why such restrictions should not be removed. In January 1996, following New York Telephone's show-cause response requesting more time for implementation, the NYSPSC issued an order requiring implementation, with respect to both residential and business services, in October 1996.

The NYSPSC has issued orders resolving various procedural and operational issues related to ILP. The NYSPSC approved New York Telephone's proposal to implement ILP for analog central offices as those switches are replaced by digital equipment. By the end of February 1996, New York Telephone had implemented ILP in all of its digital switching systems.

Other: In 1991, the NYSPSC authorized a $250 million increase in New York Telephone's rates, of which $47.5 million annually remains subject to refund pending resolution of certain issues related to New York Telephone's transactions with other NYNEX affiliates in 1984–1990. In 1995, the NYSPSC's independent consultant concluded its final report detailing findings and recommendations, and an NYSPSC administrative law judge issued a procedural ruling for future hearings and the filing of evidence. In January 1996, New York Telephone filed notice with the NYSPSC of its intention to open settlement discussions in this case and requested an extension of the date for the filing of testimony.

Federal Regulatory

Price Cap Plan: The telephone subsidiaries are subject to incentive regulation in the form of price caps. Price cap limits are subject to adjustment each year to reflect inflation, a productivity factor and certain other cost changes. In 1995, the FCC issued a Notice of Proposed Rulemaking regarding the productivity factor used by local exchange carriers ("LECs") in the FCC price cap formula. The Proposed Rulemaking will consider changes in the determination of the productivity factor, the recognition of exogenous costs, the extent of carrier sharing, and the formula for calculating the price cap index for certain services. The FCC expects to issue an order in time for the final changes to be reflected in LECs' rates as of July 1996. The FCC has also issued a Notice of Proposed Rulemaking to determine how the price cap rules should be modified to accommodate increasing levels of competition. The FCC asked for comments on a proposal by the telephone subsidiaries that earnings sharing be reduced or eliminated as an LEC implements measures to promote competition for local exchange services. The FCC has indicated that it intends to establish a rulemaking proceeding in 1996 to consider reform of the rules concerning the structure of access charges. This rulemaking proceeding would consider changes that might be necessary as competition increases in the local telephone market.

Other Federal Regulatory: In January 1996, the FCC issued a Notice of Proposed Rulemaking addressing the charges made for interconnection between LECs and wireless carriers. Currently, such charges are established by contracts under the jurisdiction of the state regulatory commissions. The FCC requested comment on its tentative conclusion to require, pending the completion of its Proposed Rulemaking, reciprocal "bill-and-keep" compensation arrangements under which the originating carrier would no longer pay the terminating carrier for access. Adoption of the proposed procedure would have a negative effect on the revenues of the LECs, including the telephone subsidiaries. The telephone subsidiaries plan to participate actively in the proceeding.

During 1996, the FCC will conduct a number of rulemaking proceedings in order to implement the Telecommunications Legislation enacted in February 1996.

In February 1996, New England Telephone advised the FCC that it relinquished authorization to construct advanced video dialtone network facilities in portions of Massachusetts and Rhode Island.

Selected Financial and Operating Data

(In millions, except per share amounts)	1995	1994	1993	1992	1991
Operating revenues	**$ 13,407**	$ 13,307	$ 13,408	$ 13,183	$ 13,255
Operating expenses	**$ 11,315**	$ 11,550	$ 13,075	$ 10,655	$ 11,665
Interest expense	**$ 734**	$ 674	$ 660	$ 685	$ 726
Earnings (loss) before extraordinary item and cumulative effect of change in accounting principle	**$ 1,069**	$ 793	$ (272)	$ 1,311	$ 601
Extraordinary item for the discontinuance of regulatory accounting principles, net of taxes	**$ (2,919)**	$ —	$ —	$ —	$ —
Cumulative effect of change in accounting for postemployment benefits, net of taxes	**$ —**	$ —	$ (122)	$ —	$ —
Net income (loss)	**$ (1,850)**	$ 793	$ (394)	$ 1,311	$ 601
Earnings (loss) per share before extraordinary item and cumulative effect of change in accounting principle	**$ 2.50**	$ 1.89	$ (.66)	$ 3.20	$ 1.49
Extraordinary item per share	**$ (6.84)**	$ —	$ —	$ —	$ —
Cumulative effect per share of change in accounting principle	**$ —**	$ —	$ (.29)	$ —	$ —
Earnings (loss) per share	**$ (4.34)**	$ 1.89	$ (.95)	$ 3.20	$ 1.49
Dividends per share	**$ 2.36**	$ 2.36	$ 2.36	$ 2.32	$ 2.28
Property, plant and equipment-net	**$ 17,055**	$ 20,623	$ 20,250	$ 19,973	$ 19,915
Total assets	**$ 26,220**	$ 30,068	$ 29,458	$ 27,732	$ 27,503
Long-term debt	**$ 9,337**	$ 7,785	$ 6,938	$ 7,018	$ 6,833
Stockholders' equity	**$ 6,079**	$ 8,581	$ 8,416	$ 9,724	$ 9,120
Book value per share	**$ 14.06**	$ 20.26	$ 20.28	$ 23.51	$ 22.38
Capital expenditures†	**$ 3,188**	$ 3,012	$ 2,717	$ 2,450	$ 2,499
Network access lines in service	**17.1**	16.6	16.0	15.6	15.3

See Management's Discussion and Analysis of Financial Condition and Results of Operations for the effect of non-recurring items on 1995 results, and restructuring charges on 1995, 1994 and 1993 results of operations. Results of operations for 1991 include $841 million of pretax ($550 million after-tax) restructuring charges.

† Excludes additions under capital lease obligations, and prior to the discontinuance of Statement No. 71, the equity component of allowance for funds used during construction.

Report of Independent Accountants

To the Share Owners and Board of Directors of NYNEX Corporation:

We have audited the accompanying consolidated balance sheets of NYNEX Corporation and its subsidiaries as of December 31, 1995 and 1994, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for each of the three years in the period ended December 31, 1995. These consolidated financial statements are the responsibility of NYNEX Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of NYNEX Corporation and its subsidiaries as of December 31, 1995 and 1994, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1995, in conformity with generally accepted accounting principles.

As discussed in Note B to the consolidated financial statements, in the second quarter of 1995, NYNEX Corporation discontinued accounting for the operations of its telephone subsidiaries in accordance with Statement of Financial Accounting Standards No. 71, "Accounting for the Effects of Certain Types of Regulation." Additionally, as discussed in Note D to the consolidated financial statements, in the fourth quarter of 1993, NYNEX Corporation adopted Statement of Financial Accounting Standards No. 112, "Employers' Accounting for Postemployment Benefits" retroactive to January 1, 1993.

Coopers & Lybrand L.L.P.
New York, New York
February 5, 1996

Report of Management

Management of NYNEX Corporation and its subsidiaries ("NYNEX") has the responsibility for preparing the accompanying consolidated financial statements and for their integrity and objectivity. The financial statements were prepared in accordance with generally accepted accounting principles, which require management to make estimates and assumptions that affect reported amounts. Actual results could differ from those estimates. In Management's opinion, the consolidated financial statements are fairly presented. Management also prepared the other information in this report and is responsible for its accuracy and consistency with the consolidated financial statements.

The consolidated financial statements have been audited by Coopers & Lybrand L.L.P. ("Coopers & Lybrand"), independent accountants, whose appointment was ratified by NYNEX's stockholders. Management has made available to Coopers & Lybrand all of NYNEX's financial records and related data, as well as the minutes of stockholders' and directors' meetings. Furthermore, Management believes that all representations made to Coopers & Lybrand during its audit were valid and appropriate.

Management of NYNEX has established and maintains an internal control structure that is designed to provide reasonable assurance as to the integrity and reliability of the consolidated financial statements, the protection of assets from unauthorized use or disposition, and the prevention and detection of fraudulent financial reporting. The concept of reasonable assurance recognizes that the cost of the internal control structure should not exceed the benefits to be derived. The internal control structure provides for appropriate division of responsibility and is documented by written policies and procedures that are communicated to employees with significant roles in the financial reporting process. Management monitors the internal control structure for compliance, considers recommendations for improvement from both the internal auditors and Coopers & Lybrand, and updates such policies and procedures as necessary. Monitoring includes an internal auditing function to independently assess the effectiveness of the internal controls and recommend possible improvements thereto. Management believes that the internal control structure of NYNEX is adequate to accomplish the objectives discussed herein.

The Audit Committee of the Board of Directors, which is comprised of directors who are not employees, meets periodically with Management, the internal auditors and Coopers & Lybrand to review the manner in which they are performing their responsibilities and to discuss matters relating to auditing, internal controls and financial reporting. Both the internal auditors and Coopers & Lybrand periodically meet privately with the Audit Committee and have access to the Audit Committee at any time.

Management also recognizes its responsibility for conducting NYNEX activities under the highest standards of personal and corporate conduct. This responsibility is accomplished by fostering a strong ethical climate as characterized in NYNEX's Code of Business Conduct, which is publicized throughout NYNEX. This code of conduct addresses, among other things, standards of personal conduct, potential conflicts of interest, compliance with all domestic and foreign laws, accountability for NYNEX property, and the confidentiality of proprietary information.

Ivan Seidenberg
Chairman and Chief Executive Officer

Peter M. Ciccone
Vice President and Comptroller