

MCLEODUSA INC  
Form DEF 14A  
August 09, 2002

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**SCHEDULE 14A INFORMATION**

Proxy Statement Pursuant to Section 14(a) of  
the Securities Exchange Act of 1934 (Amendment No. )

Filed by the Registrant   
Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to §240.14a-12

**McLeodUSA Incorporated**

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(Name of Registrant as Specified In Its Charter)

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(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- No fee required
- Fee computed on table below per Exchange Act Rules 14a-6(i)(4) and 0-11

(1) Title of each class of securities to which transaction applies:

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(2) Aggregate number of securities to which transaction applies:

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(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

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(4) Proposed maximum aggregate value of transaction:

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(5) Total fee paid:

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- Fee paid previously with preliminary materials.
- Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

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(2) Form, Schedule or Registration Statement No.:

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(3) Filing Party:

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(4) Date Filed:

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**MCLEODUSA INCORPORATED  
MCLEODUSA TECHNOLOGY PARK  
6400 C STREET SW, P.O. BOX 3177  
CEDAR RAPIDS, IOWA 52406-3177  
(319) 790-7800**

August 7, 2002

Dear Stockholder:

On behalf of the Board of Directors of McLeodUSA Incorporated, it is my pleasure to invite you to the 2002 Annual Meeting of Stockholders. The Annual Meeting will be held on Friday, September 13, 2002 at 9:30 a.m., local time, at the St. Regis Hotel, Two East 55<sup>th</sup> Street at Fifth Avenue, New York, New York.

The Annual Meeting has been called for the following purposes:

To elect 5 directors to serve on the Board of Directors;

To ratify the Board of Directors' appointment of Deloitte & Touche LLP as our independent public accountants for the 2002 fiscal year;

To approve the McLeodUSA Incorporated 2002 Omnibus Equity Plan; and

To transact such other business as may properly come before the Annual Meeting or any adjournment thereof;

all as more fully described in the accompanying Proxy Statement.

The Board of Directors has approved the matters being submitted by McLeodUSA for stockholder approval at the Annual Meeting and recommends that stockholders vote "**FOR**" each of the proposals as set forth in the attached Proxy Statement. It is important that your views be represented at the Annual Meeting. Whether or not you plan to attend the Annual Meeting, please complete and mail the enclosed proxy card or vote by telephone or through the Internet as instructed on the proxy card.

Sincerely,

/s/ CHRIS A. DAVIS

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Chris A. Davis  
*Chairman and Chief Executive Officer*

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McLeodUSA Incorporated  
McLeodUSA Technology Park  
6400 C Street SW, P.O. Box 3177  
Cedar Rapids, Iowa 52406-3177  
(319) 790-7800

**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS  
TO BE HELD ON SEPTEMBER 13, 2002**

NOTICE IS HEREBY GIVEN that the 2002 Annual Meeting of Stockholders of McLeodUSA Incorporated, a Delaware corporation, will be held on Friday, September 13, 2002 at 9:30 a.m., local time, at the St. Regis Hotel, Two East 55<sup>th</sup> Street at Fifth Avenue, New York, New York, for the following purposes:

1. To elect five directors to serve on the Board of Directors in the class of directors whose term expires in 2005;
2. To ratify the Board of Directors' appointment of Deloitte & Touche LLP as our independent public accountants for the 2002 fiscal year;
3. To approve the McLeodUSA Incorporated 2002 Omnibus Equity Plan; and
4. To transact such other business as may properly come before the Annual Meeting or any adjournment thereof;

all as more fully described in the accompanying Proxy Statement.

The foregoing items of business are more fully described in the Proxy Statement accompanying this notice.

Pursuant to our Bylaws, the Board of Directors has fixed August 2, 2002 as the record date for the determination of stockholders entitled to notice of and to vote at the Annual Meeting and at all adjournments thereof. Only stockholders of record at the close of business on that date and eligible to vote will be entitled to vote at the Annual Meeting and any adjournment thereof. A list of all stockholders entitled to vote at the Annual Meeting will be open for examination by any stockholder for any purpose germane to the Annual Meeting during ordinary business hours for a period of ten (10) days before the Annual Meeting at our offices located at 6400 C Street SW, Cedar Rapids, Iowa 52406.

By Order of the Board of Directors

/s/ CHRIS A. DAVIS

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Chris A. Davis  
*Chairman and Chief Executive Officer*

Cedar Rapids, Iowa  
August 7, 2002

*Whether or not you plan to attend the Annual Meeting, please complete and return the enclosed proxy card or vote by telephone or through the Internet as instructed on the proxy card. If you sign and return your proxy card without specifying a choice, your shares will be voted in accordance with the recommendations of the Board of Directors. You may, if you wish, revoke your proxy at any time before it is voted by filing with the Secretary of McLeodUSA a written revocation or a duly executed proxy bearing a later date, or by attending the Annual Meeting and voting in person. If you submitted your proxy by telephone or through the Internet, you may also revoke it by submitting a new proxy using the same procedures at a later date.*

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McLeodUSA Incorporated  
McLeodUSA Technology Park  
6400 C Street SW, P.O. Box 3177  
Cedar Rapids, Iowa 52406-3177

(319) 790-7800

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**PROXY STATEMENT  
2002 ANNUAL MEETING OF STOCKHOLDERS  
SEPTEMBER 13, 2002**

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**SOLICITATION, VOTING AND REVOCABILITY OF PROXIES**

This Proxy Statement and the accompanying proxy card are furnished to stockholders of McLeodUSA Incorporated entitled to vote in connection with the solicitation by the Board of Directors of McLeodUSA (the "Board of Directors") of proxies to be used at the 2002 Annual Meeting of Stockholders to be held on Friday, September 13, 2002 at 9:30 a.m., local time, at the St. Regis Hotel, Two East 55<sup>th</sup> Street at Fifth Avenue, New York, New York, and at any adjournment thereof.

If the enclosed proxy card is properly executed by a holder of shares of Class A Common Stock, Class B Common Stock, Class C Common Stock, Series A Preferred Stock or Series B Preferred Stock and returned to McLeodUSA in time to be voted at the Annual Meeting, the shares represented thereby will be voted in accordance with instructions marked thereon. **EXECUTED BUT UNMARKED PROXIES WILL BE VOTED:**

**"FOR" PROPOSAL 1 TO ELECT THE NOMINEES FOR DIRECTOR**

**"FOR" PROPOSAL 2 TO RATIFY THE APPOINTMENT OF DELOITTE & TOUCHE LLP AS OUR INDEPENDENT PUBLIC ACCOUNTANTS FOR THE 2002 FISCAL YEAR**

**"FOR" PROPOSAL 3 TO APPROVE THE MCLEODUSA INCORPORATED 2002 OMNIBUS EQUITY PLAN**

If any other matters properly come before the Annual Meeting, the persons named in the accompanying proxy will vote the shares represented by such proxies on such matters in accordance with their best judgment.

Instead of submitting a signed proxy card, stockholders may submit their proxies by telephone or through the Internet using the control number and instructions on the proxy card. Telephone and Internet proxies must be used in conjunction with, and will be subject to, the information and terms contained on the proxy card. These procedures may not be available to stockholders who hold their shares through a broker, nominee, fiduciary or other custodian.

The presence of a stockholder at the Annual Meeting will not automatically revoke such stockholder's proxy. Stockholders may, however, revoke a proxy at any time before its exercise by filing with the Secretary of McLeodUSA a written revocation or a duly executed proxy bearing a later date, or by attending the Annual Meeting and voting in person. A stockholder who submits a proxy by telephone or through the Internet may also revoke it by submitting a new proxy using the same procedures at a later date.

The cost of solicitation of proxies will be borne by us. In addition to the solicitation of proxies by mail, our officers, directors or employees also may solicit proxies personally or by telephone or other means. These persons will not be specifically compensated for the solicitation activities. Arrangements also will be made with brokerage houses and other custodians, nominees and fiduciaries for forwarding

solicitation materials to the beneficial owners of shares held of record by these persons, and we will reimburse these persons for their reasonable expenses.

This Proxy Statement, the Notice of Annual Meeting of Stockholders and the proxy card were first mailed to stockholders entitled to vote on or about August 9, 2002.

The close of business on August 2, 2002 has been fixed by the Board of Directors as the Record Date for determination of stockholders entitled to vote at the Annual Meeting. As of the Record Date, our outstanding capital stock entitled to be voted at the Annual Meeting consisted of:

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Class of Voting Securities	Number of Shares Outstanding	Number of Votes
Class A Common Stock, par value \$0.01 per share	162,499,986 shares*	Each holder of Class A Common Stock is entitled to one vote per share with respect to all matters as to which a vote is taken at the Annual Meeting.
Class B Common Stock, par value \$0.01 per share	78,203,135 shares	Each holder of Class B Common Stock is entitled to approximately 0.81454 votes per share with respect to all matters as to which a vote is taken at the Annual Meeting.**
Class C Common Stock, par value \$0.01 per share	35,546,879 shares	The holder of Class C Common Stock is entitled to approximately 1.40800 votes per share with respect to all matters as to which a vote is taken at the Annual Meeting.**
2.5% Series A Convertible Preferred Stock, par value \$0.01 per share (the "Series A Preferred Stock")	10,000,000 shares	Each holder of Series A Preferred Stock is entitled to four votes per share with respect to all matters as to which a vote is taken at the Annual Meeting.
Series B Preferred Stock, par value \$0.01 per share	10 shares	The holder of Series B Preferred Stock is entitled to one vote per share with respect to all matters as to which a vote is taken at the Annual Meeting.

\*

Includes 18,000,000 shares of Class A Common Stock held in the disputed claims reserve pursuant to the Plan of Reorganization.

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In the aggregate, the holders of the Class B Common Stock and Class C Common Stock shall be entitled to one vote per share with respect to all matters as to which a vote is taken at the Annual Meeting.

Our Bylaws provide that the holders of a *majority* of the voting rights of the shares issued and outstanding and entitled to vote shall constitute a quorum at the Annual Meeting. Stockholders' votes will be tabulated by persons appointed by the Board of Directors to act as inspectors of election for the Annual Meeting.

Assuming the presence of a quorum at the Annual Meeting:

a *plurality* of the voting rights represented and entitled to vote at the Annual Meeting is required for election of directors nominated at this annual meeting; and

a *majority* of the voting rights represented and entitled to vote at the Annual Meeting is required to ratify the appointment of Deloitte & Touche LLP as our independent public accountants and to approve the McLeodUSA Incorporated 2002 Omnibus Equity Plan.

Unless otherwise required by applicable law or our Second Amended and Restated Certificate of Incorporation (the "Certificate of Incorporation") or Bylaws, the affirmative vote of a *majority* of the

voting rights represented and entitled to vote at the Annual Meeting is required to decide any other matter submitted to a stockholder vote. Our Certificate of Incorporation does not provide for cumulative voting in the election of directors.

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Abstentions and broker non-votes will be treated as shares that are present, in person or by proxy, and entitled to vote for purposes of determining the presence of a quorum at the Annual Meeting. Broker non-votes will not be counted as present or entitled to vote on any matter presented at the Annual Meeting. As a result, broker non-votes will not have any effect on Proposal 1, 2 or 3. Abstentions will be counted as shares that are present and entitled to vote on matters presented at the Annual Meeting. As a result, abstentions will not have any effect on Proposal 1 but will have the same effect as a vote *against* Proposal 2 or Proposal 3.

### McLeodUSA's Plan of Reorganization

On April 16, 2002 (the "Effective Date"), the First Amended Plan of Reorganization of McLeodUSA Incorporated (the "Plan of Reorganization") became effective and McLeodUSA emerged from Chapter 11 protection. The Plan of Reorganization, which resulted in a change of control of McLeodUSA, effected the following changes to McLeodUSA's capital structure:

The elimination of the approximately \$3 billion of indebtedness represented by the outstanding notes (including the 10<sup>1</sup>/<sub>2</sub>% Senior Discount Notes, 9<sup>1</sup>/<sub>4</sub>% Senior Notes, 8<sup>3</sup>/<sub>8</sub>% Senior Notes, 9<sup>1</sup>/<sub>2</sub>% Senior Notes, 8<sup>1</sup>/<sub>8</sub>% Senior Notes, 12% Senior Notes, 11<sup>1</sup>/<sub>2</sub>% Senior Notes and 11<sup>3</sup>/<sub>8</sub>% Senior Notes (collectively, the "Notes"));

In exchange for the cancellation of the Notes, the distribution to bondholders of their pro rata share of (i) \$670 million in cash, (ii) 10,000,000 shares of Series A Preferred Stock and (iii) 5-year warrants to purchase 22,159,091 shares of Class A Common Stock for \$30 million in the aggregate;

The investment by two funds affiliated with Forstmann Little & Co. of \$175 million in exchange for (i) 74,027,764 shares of Class A Common Stock, (ii) 5-year warrants to purchase 22,159,091 shares of Class A Common Stock for \$30 million in the aggregate and (iii) 10 shares of Series B Preferred Stock;

The conversion of old Series D Preferred Stock and old Series E Preferred Stock, held by three funds affiliated with Forstmann Little & Co., into 78,203,135 shares of Class B Common Stock and 35,546,879 shares of Class C Common Stock, respectively; and

The conversion of old Series A preferred stock into 33,696,559 shares of Class A Common Stock.

The Plan of Reorganization also provided for the distribution of a portion of reorganized McLeodUSA's common stock to holders of old common stock. These holders were entitled to share, together with holders of certain securities claims, in the distribution of 54,775,663 shares of reorganized McLeodUSA Class A Common Stock.

*Stock issued and outstanding:* Under the Plan of Reorganization, the outstanding common stock and preferred stock and all of the Notes were cancelled on the Effective Date. On April 17, 2002, McLeodUSA distributed the cash, new Series A Preferred Stock and warrants to holders of the Notes and distributed the shares of reorganized McLeodUSA common stock to holders of the old preferred stock. No distribution of reorganized McLeodUSA common stock was made to holders of old common stock pending a determination of a disputed claims reserve with respect to any securities claims entitled to share in such distribution. On May 2, 2002, the Bankruptcy Court entered an order establishing a disputed claims reserve at 18,000,000 shares of reorganized McLeodUSA Class A Common Stock pending resolution of the securities claims associated with the putative securities class actions. McLeodUSA then commenced distribution of 36,775,663 shares of reorganized McLeodUSA Class A

Common Stock to record holders of old common stock as of April 5, 2002, the distribution record date under the Plan of Reorganization. Upon the final determination of the amount, if any, of allowed securities claims under the Plan of Reorganization, such holders of old common stock may be entitled to additional distributions of reorganized McLeodUSA Class A Common stock from the 18,000,000 shares held in the disputed claims reserve.

For a more detailed discussion of the Plan of Reorganization, see "Business Recent Transactions" in McLeodUSA's Annual Report on Form 10-K/A. Also, see "STOCK OWNERSHIP BY MANAGEMENT AND MORE THAN 5% STOCKHOLDERS" in this Proxy Statement.

**THE BOARD OF DIRECTORS RECOMMENDS THAT STOCKHOLDERS VOTE "FOR" APPROVAL OF THE PROPOSALS SET FORTH IN THIS PROXY STATEMENT.**

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**ELECTION OF DIRECTORS  
(Proposal 1)**

The Board of Directors currently consists of fifteen directors, divided into three classes of directors serving staggered three-year terms. At the Annual Meeting, five directors will be elected to serve as Class I directors whose term expires in 2005.

The Board of Directors has nominated the following for director:

Thomas D. Bell, Jr., Edward D. Breen, Dale F. Frey, Stephen C. Gray and Jeong H. Kim, each for a three-year term.

Unless otherwise specified on the proxy card, it is the intention of the persons named in the proxy to vote the shares represented by each properly executed proxy for the election as directors of Messrs. Thomas D. Bell, Jr., Edward D. Breen, Dale F. Frey, Stephen C. Gray and Jeong H. Kim. The Board of Directors believes that such nominees will stand for election and will serve if elected. If any person nominated by the Board of Directors fails to stand for election or is unable to accept election, the proxies will be voted for the election of such other person or persons as the persons named in the accompanying proxy shall determine in accordance with their best judgment. Pursuant to our Certificate of Incorporation, directors are elected by plurality vote.

Our Bylaws provide that the Board of Directors shall consist of not fewer than seven directors nor more than fifteen directors and that the number of directors, within such limits, shall be determined by resolution of the Board of Directors. However, the Bylaws also provide that the Board of Directors will have as members at least (a) five "independent directors," (b) three officers of McLeodUSA selected by the Board of Directors; provided that each such officer shall hold one or more of the following titles: Chairperson; Chief Executive Officer; President; Chief Operating Officer or Chief Financial Officer, (c) the designee of the Series A Preferred Stock, if any (as discussed below), and (d) the designee(s) of the Series B Preferred Stock, if any (as discussed below).

Pursuant to the Amended and Restated Purchase Agreement, dated as of January 30, 2002, as amended (the "Purchase Agreement"), the funds affiliated with Forstmann Little & Co. which hold McLeodUSA stock agreed that during the period from the closing of the Purchase Agreement until the "Standstill Termination Date," such funds will be present, in person or by proxy, at all meetings of our stockholders so that all of their voting securities are counted for purposes of determining the presence of a quorum at such meetings. Such funds also agreed that, during such period, they will vote their McLeodUSA voting securities in all elections of directors such that the persons specified in clauses (a) and (b) above are elected as members to the Board of Directors. The "Standstill Termination Date" means the earlier of the close of business on the day preceding the third anniversary of the closing of the Purchase Agreement or the date Theodore J. Forstmann is removed, without his consent, as the Chairman of the Executive Committee of the Board of Directors.

*Series A Preferred Stock Designee*

The Certificate of Designation for the Series A Preferred Stock provides that for as long as 3,333,333 shares of Series A Preferred Stock remain outstanding, the holders of Series A Preferred Stock will have the right to designate one member of the Board of Directors.

*Series B Preferred Stock Designee(s)*

The Certificate of Designation for the Series B Preferred Stock and the Purchase Agreement provide certain funds affiliated with Forstmann Little & Co. (the "Forstmann Funds") with the right to designate members of the Board of Directors and/or non-voting observers to the Board of Directors as follows:

As long as the Forstmann Funds beneficially own at least 40% of the McLeodUSA common stock they received upon consummation of the Plan of Reorganization, the Forstmann Funds will have the right to designate two members of the Board of Directors.

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As long as the Forstmann Funds beneficially own less than 40%, but more than 20%, of such shares, the Forstmann Funds will have the right to designate one member of the Board of Directors and one non-voting observer to the Board of Directors.

Once the Forstmann Funds beneficially own 20% or less of such shares, the Forstmann Funds will have no rights to designate members of the Board of Directors; but, as long as the Forstmann Funds beneficially own any of such shares, the Forstmann Funds will have the right to designate two non-voting observers to the Board of Directors.

The Purchase Agreement also provides the other Forstmann Little & Co. funds that beneficially own McLeodUSA securities with the right to designate observers to the Board of Directors as necessary to maintain the venture capital operating company status of their investment in McLeodUSA.

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE "FOR" THE ELECTION OF THE NOMINEES FOR DIRECTORS.**

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**Information as to Nominees, Continuing Directors and Executive Officers**

The following table sets forth information regarding the Board of Directors' five nominees for election as directors, those directors who will continue to serve as such after the Annual Meeting and the Executive Officers.

Nominees:	Age at August 5, 2002	Director Since	Term Expiring	Position(s) Held with the Company
<b>Class I</b>				
Thomas D. Bell, Jr. (2)	52	2001	2005	Director
Edward D. Breen (2)(3)	46	2001	2005	Director
Dale F. Frey (1)(3)	69	2001	2005	Director
Stephen C. Gray (3)	44	1993	2005	President and Director
Jeong H. Kim	41	2002	2005	Director
<b>Continuing Directors:</b>				
<b>Class II</b>				
G. Kenneth Burckhardt	47	2002	2003	Executive Vice President and Chief Financial Officer and Director
James E. Hoffman	49	2000	2003	Director
Farid Suleman (1)	50	2002	2003	Director
Peter V. Ueberroth (2)	64	2001	2003	Director
Juan Villalonga	49	2002	2003	Director
<b>Class III</b>				
Jeffrey D. Benjamin (4)	41	2002	2004	Director
Thomas M. Collins (1)	74	1993	2004	Director
Chris A. Davis (3)	51	2001	2004	Chairman of the Board of Directors and Chief Executive Officer
Theodore J. Forstmann (3)(5)	62	1999	2004	Director and Chairman of the Executive Committee of the Board of Directors
Thomas H. Lister (2)(3)(5)	38	2001	2004	Director



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- (1) Currently a member of the Audit Committee.
- (2) Currently a member of the Compensation Committee.
- (3) Currently a member of the Executive Committee.
- (4) Selected as a director by the holders of Series A Preferred Stock.
- (5) Selected as a director by the holders of Series B Preferred Stock.

The principal occupations for the past five years of each of the five nominees for director, the ten directors whose terms of office will continue after the Annual Meeting and the listed Executive Officers are set forth below.

Chris A. Davis  
Chairman of the Board of Directors and Chief Executive Officer

Ms. Davis has been Chairman and Chief Executive Officer since April 2002. She joined McLeodUSA in August 2001 as Chief Operating and Financial Officer, member of the Board of Directors, and member of the Board's Executive Committee. She previously served as Executive Vice President and Chief Financial and Administrative Officer of ONI Systems from May 2000 to August 2001. She was

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Executive Vice President and Chief Financial Officer, and a member of the Board of Directors, for Gulfstream Aerospace Corporation from May 1993 to April 2000. Before joining Gulfstream in 1993, Ms. Davis spent 17 years at General Electric Company, where she held various managerial and executive positions. Ms. Davis also serves on the Board of Directors for Cytec Industries Inc., Rockwell Collins, Inc. and Wolverine Tube, Inc.

Stephen C. Gray  
President and Director

Mr. Gray has been an officer and a director of McLeodUSA since 1993. Prior to joining McLeodUSA, Mr. Gray served from August 1990 to September 1992 as Vice President of Business Services at MCI, where he was responsible for MCI's local access strategy and for marketing and sales support of the Business Markets division. From February 1988 to August 1990, he served as Senior Vice President of National Accounts and Carrier Services for Telecom\*USA, where his responsibilities included sales, marketing, key contract negotiations and strategic acquisitions and combinations. From September 1986 to February 1988 Mr. Gray held a variety of management positions with Williams Telecommunications Company.

G. Kenneth Burckhardt  
Executive Vice President and Chief Financial Officer and Director

Mr. Burckhardt was named Executive Vice President and Chief Financial Officer, and also elected to the McLeodUSA Board of Directors, in April 2002. Prior to joining McLeodUSA, Mr. Burckhardt was interim CFO at ONI Systems, a leading optical networking company, from August 2001 to February 2002 and served as Vice President Finance from May 2000 to August 2001. From December 1994 to May 2000, he worked at Gulfstream Aerospace Corporation, most recently as Senior Vice President, Finance. From 1977 to 1994, he held various financial management positions at the General Electric Company.

Thomas D. Bell, Jr.  
Director

Mr. Bell has served as a director of McLeodUSA since August 2001. Mr. Bell serves as President and CEO of Cousins Properties Incorporated. From January 2001 to July 2001, Mr. Bell was a Special Limited Partner of Forstmann Little & Co. Mr. Bell is the former Chairman and CEO of Young & Rubicam, a leading global marketing services firm. Earlier in his career, he was President and CEO of Burson-Marsteller, a leading

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public relations firm, Vice Chairman of Gulfstream Aerospace and Executive Vice President of Ball Corporation. He is a director on the boards of Lincoln Financial Group, Cousins Properties Inc., Regal Entertainment Group and Credit Suisse Group.

Jeffrey D. Benjamin  
Director

Mr. Benjamin was named to the McLeodUSA Board of Directors in April 2002. He has been Managing Director of Libra Securities LLC, an investment banking firm, since January 2002. He has been employed by Libra Securities LLC and its predecessors since May 1998, serving in various capacities including Co-Chief Executive Officer. From May 1996 to May 1998, Mr. Benjamin was Managing Director at UBS Securities LLC, an investment banking firm. He is also a director of Chiquita Brands International, Inc. and EXCO Resources, Inc.

Edward D. Breen  
Director

Mr. Breen has served as a director of McLeodUSA since August 2001. In July 2002, Mr. Breen was named Chairman and Chief Executive Officer of Tyco International Ltd. Until July 2002, Mr. Breen was President and Chief Operating Officer of Motorola, Inc. Prior to becoming President and Chief

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Operating Officer, he had served as Executive Vice President and President of Motorola and President of its Networks Sector, and as President and Chief Executive Officer of General Instrument Corporation from 1997 until it was acquired by Motorola in 2000. Mr. Breen is a director of CommScope, Inc. and Tyco International Ltd.

Thomas M. Collins  
Director

Mr. Collins has served as a director of McLeodUSA since April 1993. Mr. Collins is Of Counsel and Past Chairman of Shuttleworth & Ingersoll, P.C., a law firm in Cedar Rapids, Iowa, where he had practiced law since 1952. Mr. Collins was a director of Teleconnect and its successor, Telecom\*USA, from 1985 to August 1990. He is also a director of APAC Customer Services, Inc., a provider of customer relationship management services.

Theodore J. Forstmann  
Chairman of the Executive Committee of the Board of Directors

Mr. Forstmann was appointed Chairman of the Executive Committee of the McLeodUSA Board of Directors in August 2001. He has served as a director of McLeodUSA since September 1999. Mr. Forstmann is co-founder and senior partner of Forstmann Little & Co., a major New York private equity firm that has invested about \$12 billion in 29 acquisitions in the past two decades. Forstmann Little's best-known acquisitions include Gulfstream Aerospace, General Instrument, Ziff-Davis Publishing, Community Health Systems, Yankee Candle, Dr. Pepper and Topps. Mr. Forstmann serves as a director of Community Health Systems, Yankee Candle Company and Citadel Communications.

Dale F. Frey  
Director

Mr. Frey has served as a director of McLeodUSA since August 2001. Mr. Frey is retired from General Electric and General Electric Investment Corporation, where he served in various executive positions, including Chairman of the Board and President of GEI and Vice President and Treasurer of GE. In addition, he served in a number of managerial positions in Finance in the Aerospace and Defense, Aircraft Engine and Power Delivery businesses at GE. He also served as Staff Executive-International Finance Operation. Mr. Frey is a veteran of the U.S. Air Force. He is a member of the Boards of Directors of Yankee Candle Company, Aftermarket Technology Corp., Community Health Systems, Praxair, Inc., Roadway Express, Inc., Invemed Catalyst Fund and Vantis Equity Associates. He serves as a member of the Forstmann Little & Co. and Aurora Capital Advisory Committees. Mr. Frey is the Chairman of the Damon Runyon Cancer Research Foundation, a member of the Board of Overseers of New York University Leonard N. Stern School of Business and a trustee of Franklin and Marshall College.

James E. Hoffman  
Director

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Mr. Hoffman has served as a director of McLeodUSA since May 2000. Mr. Hoffman is Executive Vice President Business Development for Alliant Energy Corporation. Since April 1998, he has been President of Alliant Energy Resources, Inc., a wholly owned subsidiary of Alliant Energy Corporation. He previously served in a number of executive positions at Alliant Energy, including President of Alliant Energy Resources, Inc. Prior to joining Alliant Energy in 1995, Mr. Hoffman served as Chief Information Officer for MCI Communications. He also served as Executive Vice President of Telecom\*USA.

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Jeong H. Kim  
Director

Jeong H. Kim, Ph.D. was elected a director of McLeodUSA in May 2002. He was most recently President of the Optical Networking Group at Lucent Technologies, which he joined in 1998 after Lucent acquired Yurie Systems for \$1.1 billion. He founded Yurie Systems, a high-tech communications equipment company in 1992, and served as Chairman and CEO until its acquisition by Lucent. His early career encompassed computer design, satellite systems design and data communications, and included seven years as a Nuclear Submarine Officer in the U.S. Navy. He holds a Ph.D. in Reliability Engineering from the University of Maryland, and a Master's Degree in Technical Management from Johns Hopkins University. Among his service commitments, Kim served on an eight member Presidential Commission on Review of U.S. Intelligence. He currently serves on the boards of In-Q-Tel, Stanford University's Institute for International Studies, the Johns Hopkins University, the University of Maryland College Park Foundation and GIV Global Private Equity.

Thomas H. Lister  
Director

Mr. Lister has served as a director of McLeodUSA since November 2001. Mr. Lister became a general partner of Forstmann Little & Co. in 1997, after joining the firm as an associate in 1993. Mr. Lister worked in the Mergers & Acquisitions Department at Morgan Stanley from 1986 to 1989 and again from 1991 to 1993. He is also a director of Community Health Systems.

Farid Suleman  
Director

Farid Suleman was elected a director of McLeodUSA in May 2002. He has been the CEO of Citadel Communications and a Special Limited Partner of Forstmann Little & Co. since March 2002. Prior to joining Forstmann Little, he was President and CEO of Infinity Broadcasting Corp., one of the largest radio broadcasting and outdoor advertising companies in America. He was previously Executive Vice President, Chief Financial Officer, Treasurer and Director of Infinity Broadcasting Corp. and also Senior Vice President of CBS Station Group. Suleman is a Director of Westwood One and was also Westwood One's Executive Vice President and Chief Financial Officer.

Peter V. Ueberroth  
Director

Mr. Ueberroth has served as a director of McLeodUSA since August 2001. Mr. Ueberroth is the Managing Director of Contrarian Group, Inc., an investment and management company, and is Owner and Co-Chairman of the Pebble Beach Company. He also serves as the Chairman of the Board of Ambassadors International. He previously served as the Commissioner of Major League Baseball and as President of the Los Angeles Olympic Organizing Committee, the private non-profit organization responsible for staging and operating the 1984 Los Angeles Olympic Games. In 1962, Mr. Ueberroth founded First Travel Company, which grew to become the second largest travel business in North America with over 300 wholly owned retail travel agencies when it was sold in 1980. He serves on the boards of Ambassadors International, Bank of America Corporation, The Coca-Cola Company, and Hilton Hotels Corporation.

Juan Villalonga  
Director

Juan Villalonga was elected to the McLeodUSA Board of Directors in May 2002. He most recently served as Chairman and CEO of Telefónica Group from 1996 to 2000, and was instrumental in Telefónica's transformation into one of Europe's four largest telecommunications companies and the leading telecommunications company in Latin America. While at Telefónica, Villalonga also created the Internet portal Terra Networks, and led its \$12.5 billion acquisition of U.S. portal Lycos. Previously, he headed the activities of Bankers Trust Company in Spain and Portugal, and was CEO of Credit Suisse

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First Boston in Spain. Earlier in his career, he was a partner at the international consulting firm McKinsey & Co., where he worked for nine years throughout the United States, Portugal, Spain and Italy. He serves on the Boards of Univision and Banco Espirito Santo Group, and is a member of the Advisory Board of Ben Gurion University.

### **Corporate Governance and Related Matters**

The Board of Directors conducts its business through meetings and through its committees. The Executive Committee of the Board of Directors acts as a nominating committee for selecting candidates to stand for election as directors. Pursuant to our Bylaws, other candidates also may be nominated by any stockholder, provided such other nomination(s), together with the identity of the nominator and the number of shares of McLeodUSA stock owned, directly and indirectly, by the nominator, are submitted in writing to the Secretary of McLeodUSA not less than 60 days and not more than 90 days prior to the anniversary date of the immediately preceding annual meeting of stockholders, provided, however, that in the event that the annual meeting is called for a date that is not within thirty days before or after such anniversary date, notice by the stockholder must be received not later than the close of business on the tenth day following the day on which the notice of the date of the annual meeting was mailed or such public disclosure of the date of the annual meeting was made, whichever first occurs. No such nominations have been received as of the date of this Proxy Statement in connection with the Annual Meeting.

The Board of Directors has established an Executive Committee, an Audit Committee and a Compensation Committee.

*The Executive Committee.* The Executive Committee was established in July 2000 and its current members are Ms. Davis and Messrs. Gray, Breen, Forstmann, Frey and Lister. The Executive Committee has and may exercise all of the powers and authority of the Board of Directors in the management of the business and affairs of McLeodUSA to the fullest extent permitted by applicable law. Mr. Forstmann serves as the Chairman of the Executive Committee.

*The Audit Committee.* The Audit Committee, among other things, recommends the firm to be appointed as independent public accountants to audit our financial statements, discusses the scope and results of the audit with the independent public accountants, reviews with management and the independent public accountants our interim and year-end operating results, considers the adequacy of our internal accounting controls and audit procedures and reviews the non-audit services to be performed by the independent public accountants. The current members of the Audit Committee are Messrs. Collins, Frey and Suleman. The Board of Directors amended and restated in December 2000 the written charter for the Audit Committee. In addition, the Board of Directors has determined that the members of the Audit Committee meet the independence requirements of the National Association of Securities Dealers. Mr. Frey serves as Chairman of the Audit Committee.

*The Compensation Committee.* The Compensation Committee reviews and recommends the compensation arrangements for management and administers McLeodUSA's stock option plan. The current members of the Compensation Committee are Messrs. Bell, Breen, Lister and Ueberroth. Mr. Breen serves as Chairman of the Compensation Committee.

During the fiscal year ended December 31, 2001, the Board of Directors met or acted by unanimous consent 12 times. During the same period, the Executive Committee met 9 times, the Audit Committee met 5 times and the Compensation Committee met 9 times. During the fiscal year ended December 31, 2001, no director attended fewer than 75% of the total of all meetings of the Board of Directors and any committee on which the director served.

### **Directors' Compensation**

Our directors who are also employees receive no directors' fees. Non-employee directors receive directors' fees of \$1,000 for each Board and committee meeting attended in person and \$500 for each

Board and committee meeting attended by telephone. In addition, directors are reimbursed for reasonable out-of-pocket travel expenditures incurred in connection with their attendance at Board and committee meetings.

During fiscal year 2001, directors were also eligible to receive grants of stock options under the Directors Stock Option Plan (the "Directors' Plan") and the 1996 Employee Stock Option Plan, as amended. Under the Directors' Plan, an aggregate of 6,600,000 shares of Class A common stock, par value \$0.01 per share (the "Old Class A common stock") were reserved for purchase pursuant to option grants to McLeodUSA directors who are not officers or employees. Options for 4,810,000 shares of Old Class A common stock had been granted under

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the Directors' Plan and options to purchase 2,613,750 shares of Old Class A common stock had been exercised as of December 31, 2001. Each eligible director who commenced service as a director was granted an initial option to purchase up to 120,000 shares of Old Class A common stock under the Directors' Plan. Each eligible director was also granted additional options to purchase up to 60,000 shares of Old Class A common stock after each subsequent annual meeting of stockholders under the Directors' Plan. In addition, eligible directors could be granted such discretionary options under the Directors' Plan, in addition to the foregoing options, as determined by the Board; provided that no more than an aggregate of 600,000 shares of Old Class A common stock could be granted as discretionary options. On April 16, 2002, the effective date of the Plan of Reorganization, all outstanding options under the Directors' Plan were cancelled and the Directors' Plan was replaced by the McLeodUSA Incorporated 2002 Omnibus Equity Plan (the "Omnibus Plan").

As of December 31, 2001, 1,770,000 options had been granted to non-employee directors under the McLeodUSA 1996 Employee Stock Option Plan, none of which had been exercised. On April 16, 2002, the effective date of the Plan of Reorganization, all outstanding options under the 1996 Employee Stock Option Plan were cancelled, and the 1996 Employee Stock Option Plan was replaced by the Omnibus Plan.

Other than the compensation described above, none of the directors received any compensation from McLeodUSA in 2001 in connection with their service as directors. Effective as of April 16, 2002 (the effective date of the Plan of Reorganization), directors became eligible to receive awards under the Omnibus Plan, which was adopted in accordance with the Plan of Reorganization. See "APPROVAL OF THE MCLEODUSA INCORPORATED 2002 OMNIBUS EQUITY PLAN (Proposal 3) Description of the McLeodUSA Incorporated 2002 Omnibus Equity Plan."

Pursuant to the Omnibus Plan, the Compensation Committee adopted on April 18, 2002 (and the Board of Directors ratified and confirmed on April 24, 2002) a general policy for granting stock options to directors. The policy provides that non-employee directors will be granted, on a one-time basis, options to acquire 300,000 shares, plus an additional 100,000 options for each committee on which a director serves, plus an additional 325,000 options for serving as chair of the Executive Committee, and upon resignation such directors will have one year to exercise any options which are vested at the time of resignation. The policy also provides that stock options for such directors serving at the time of establishment of the policy will vest 25% on the date of grant and 25% per year for the following three years and that stock options for such directors subsequently elected or appointed would vest one-third on each of the first three years following the date of grant and, in either case, the options would vest fully upon a change of control. The non-employee directors serving on April 18, 2002 were granted options in accordance with the policy, including Messrs. Hesse and Claudy who have each subsequently resigned. On April 18, 2002, Mr. McLeod and Mr. Wilkens were granted options to acquire 500,000 shares and 300,000 shares, respectively, which vested 25% upon date of grant and 25% per year for the following three years and which provided that such options would fully vest upon retirement and that such options could be exercised for a period of one-year following either retirement or the end of the term of their current employment agreement, whichever is later. Mr. McLeod and Mr. Wilkens have each subsequently retired.

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### EXECUTIVE COMPENSATION AND OTHER INFORMATION

#### Executive Compensation

The following table sets forth a summary of the compensation paid during 2001, 2000 and 1999 for services rendered in all capacities to McLeodUSA and its subsidiaries by certain of our past and present executive officers (namely, "Named Executive Officers"):

Name and Principal Position	Year	Annual Compensation			Other Annual Compensation	Long-Term Compensation Awards Underlying Options (1)	All Other Compensation (2)
		Salary	Bonus				
Clark E. McLeod(12) Chairman, Director	2001	\$ 400,000	\$ 82,350(11)			\$ 1,883,400(3)	
	2000	397,692	166,651		3,000,000(10)	1,883,400(3)	
	1999	250,000	142,000			1,883,200(3)	
Stephen C. Gray President, Chief Executive	2001	\$ 400,000	\$ 82,350(11)	8,954		3,400	
	2000	397,692	166,651		6,000,000(10)	3,400	

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		Annual Compensation			Long-Term Compensation	
					Awards	
					Underlying	
					Options (1)	
Officer and Director	1999	250,000	142,000		3,000,000	3,200
Chris A. Davis(4)	2001	153,846	8,186,398	3,014	6,000,000	2,207,325(6)
Chairman and Chief Executive	2000					
Officer and Director	1999					
Roy A. Wilkens(5)	2001	206,000	77,557(11)			
President and Chief Executive	2000	393,846	117,736		6,000,000(10)	
Officer Network Services and Director	1999				180,000	
Arthur L. Christoffersen(13)	2001	200,000	394,500(9)	3,900	50,000	3,400
President and Chief Executive	2000	200,000	90,000	4,050	390,000	3,400
Officer Publishing Services	1999	180,000	110,000	20,035	450,000	3,200
Randall Rings(14)	2001	170,000	284,376(9)		40,000	3,400
Group Vice President Law and Secretary	2000	160,000	209,634		300,000	3,217
	1999	116,538	61,728		720,000	3,200
Blake O. Fisher, Jr.(15)	2001	180,000	302,214(9)		30,000	3,474(7)
Group Vice President Planning and Development	2000	179,999	236,288		120,000	3,400
	1999	175,000	102,680		360,000	342,690(8)

(1) On April 16, 2002, the effective date of the Plan of Reorganization, all outstanding options were cancelled.

(2) Unless otherwise indicated, all other compensation represents matching contributions made by McLeodUSA to the McLeodUSA Incorporated 401(k) Plan on behalf of the applicable individual.

(3) For 2000 and 1999, includes \$1,880,000 of premiums paid on split dollar life insurance policies for the benefit of the McLeod Family 1998 Special Trust. In January 2002, McLeodUSA and the trustees of The McLeod Family 1998 Special Trust entered into a modification and restatement of the split dollar agreement pursuant to which the trustees made a payment to McLeodUSA in the amount of \$2,700,000 in exchange for the release of McLeodUSA's collateral assignments on the existing policies and for the agreement of McLeodUSA to make a single further premium payment of \$1,880,000 (the payment otherwise due in December 2001 under the split dollar agreement, as modified) to acquire additional insurance on the lives of Clark and Mary McLeod. As a result of this modification and restatement, McLeodUSA was fully released from its obligations to make future payments under such agreement. For additional information, see "Certain Relationships and Related Transactions."

(4) Ms. Davis joined McLeodUSA as Chief Operating and Financial Officer and Director in August 2001 and became Chairman and Chief Executive Officer on April 24, 2002.

(5) Mr. Wilkens resigned as an officer in the fourth quarter of 2001 and as a director in May 2002.

(6)

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Includes \$2,207,325 paid by McLeodUSA to Ms. Davis for reimbursement of relocation expenses and a gross-up payment for associated taxes (including proceeds and gross-up related to the sale of Ms. Davis' home).

- (7) Includes \$74 paid by McLeodUSA to Mr. Fisher for reimbursement of relocation expenses.
- (8) Includes \$339,490 paid by McLeodUSA to Mr. Fisher for reimbursement of relocation expenses.
- (9) Includes the fair market value (utilizing the Black-Scholes valuation method) of stock options issued in lieu of a cash bonus on May 7, 2001 in the amount of \$294,500 for Mr. Christoffersen, \$250,325 for Mr. Rings and \$265,050 for Mr. Fisher. These options were granted with an exercise price of \$6.03, which was the closing price of the Old Class A common stock on the day prior to the grant. On the effective date of the Plan of Reorganization, all options granted during 2001 were cancelled.
- (10) These options were cancelled during 2001.
- (11) Amount paid in 2001 pursuant to bonus plan in effect for performance during 2000. No cash bonus was paid for performance during 2001.
- (12) Mr. McLeod retired from his position as Chairman and Director in April 2002.
- (13) In April 2002, upon the sale of the publishing business, Mr. Christoffersen ended his service as an officer of McLeodUSA.
- (14) Mr. Rings resigned as an officer effective July 20, 2002.
- (15) Mr. Fisher resigned as an officer effective May 15, 2002.

### Stock Option Grants in the 2001 Fiscal Year

The following table sets forth information relating to stock options granted during the fiscal year ended December 31, 2001 to the Named Executive Officers. On April 16, 2002, the effective date of the Plan of Reorganization, all options granted during 2001 were cancelled.

Name	Number of Securities Underlying Options Granted (5)	Percent of Total Options Granted to Employees in Fiscal Year	Exercise Price	Grant Date	Expiration Date	Potential Realized Value at Assumed Annual Rates of Stock Price Appreciation for Option Term	
						5%	10%
Clark E. McLeod(6)							
Stephen C. Gray							
Chris A. Davis	6,000,000(4)	24.78%	\$ 1.12	August 29, 2001	August 29, 2011	\$ 4,226,172	\$ 10,709,949
Roy A. Wilkens(3)							
Arthur L. Christoffersen(7)	50,000(1)	.21%	\$ 6.03	May 7, 2001	May 7, 2011	\$ 189,612	\$ 480,513
Christoffersen(7)	50,000(2)	..21%	\$ 6.03	May 7, 2001	May 7, 2011	\$ 189,612	\$ 480,513
Randall Rings(8)	40,000(1)	.17%	\$ 6.03	May 7, 2001	May 7, 2011	\$ 151,689	\$ 384,411
	42,500(2)	..18%	\$ 6.03	May 7, 2001	May 7, 2011	\$ 161,170	\$ 408,436
Blake O. Fisher, Jr.(9)	30,000(1)	.12%	\$ 6.03	May 7, 2001	May 7, 2011	\$ 113,767	\$ 288,308
	45,000(2)	..19%	\$ 6.03	May 7, 2001	May 7, 2011	\$ 170,651	\$ 432,462

(1)

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These options vested according to the following schedule: 25% per year for four years commencing on January 2, 2002.

- (2) These options vested according to the following schedule: 25% on July 1, 2001, 25% on October 1, 2001 and 50% on January 1, 2002.
- (3) Mr. Wilkens resigned as an officer in the fourth quarter of 2001 and as a director in May 2002.
- (4) These options vested according to the following schedule: 25% immediately and 25% per year for the next three years.
- (5) On the effective date of the Plan of Reorganization, all options granted during 2001 were cancelled.
- (6) Mr. McLeod retired from his position as Chairman and Director in April 2002.
- (7) In April 2002, upon the sale of the publishing business, Mr. Christoffersen ended his service as an officer of McLeodUSA.
- (8) Mr. Rings resigned as an officer effective July 20, 2002.
- (9) Mr. Fisher resigned as an officer effective May 15, 2002.

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### Fiscal Year-end Option Values

The following table sets forth information for each Named Executive Officer concerning the exercise of options during fiscal year 2001, the number of securities underlying unexercised options at the 2001 year-end and the year-end value of all unexercised in-the-money options held by such individuals. On April 16, 2002, the effective date of the Plan of Reorganization, all outstanding options were cancelled.

Name	Shares Acquired on Exercise	Value Realized	Number of Unexercised Options at Fiscal Year-end(4)		Value of Unexercised In-the-Money Options at Fiscal Year-End(1)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Clark E. McLeod (5)		\$	956,002	331,998	\$	\$
Stephen C. Gray		\$	2,454,762	3,246,750	\$	36,222
Chris A. Davis (2)		\$	1,500,000	4,500,000	\$	\$
Roy A. Wilkens (3)		\$	162,249	90,000	\$	\$
Arthur L. Christoffersen (6)		\$	572,001	1,068,000	\$	\$
Randall Rings(7)		\$	182,447	1,070,749	\$	\$
Blake O. Fisher, Jr.(8)		\$	1,049,054	694,998	\$	\$

- (1) Represents the difference between the exercise price and the closing price of McLeodUSA Class A common stock on the NASDAQ National Market on December 31, 2001.
- (2) Ms. Davis did not join McLeodUSA or receive an option grant until August 2001.
- (3) Mr. Wilkens resigned as an officer in the fourth quarter of 2001 and as a director in May 2002.
- (4) On the effective date of the Plan of Reorganization, all outstanding options were cancelled.



- (5) Mr. McLeod retired from his position as Chairman and Director in April 2002.
- (6) In April 2002, upon the sale of the publishing business, Mr. Christoffersen ended his service as an officer of McLeodUSA.
- (7) Mr. Rings resigned as an officer effective July 20, 2002.
- (8) Mr. Fisher resigned as an officer effective May 15, 2002.

#### **Bonus Plan and Other Benefit Programs**

McLeodUSA has a contributory retirement plan (the "401(k) Plan") for its employees (including executive officers) age 21 and over with at least three months of service with McLeodUSA. The 401(k) Plan provides that each participant may contribute up to 50% (the limit was 15% for 2001 and prior years) of his or her salary (not to exceed the annual statutory limit). During 2001, McLeodUSA made matching contributions to each participant's account equal to 50% of the participant's contribution up to 2% of the participant's annual compensation. In addition, McLeodUSA may make a discretionary annual match of up to another 50% of the participant's contribution up to 2% of the participant's annual compensation. Thus, the total matching contribution can be up to 4% of the participant's annual compensation. Although McLeodUSA makes such matching contributions in McLeodUSA common stock, employees are otherwise prohibited from purchasing McLeodUSA common stock with their own contributions to the 401(k) Plan. No discretionary annual match was made for 2001. In addition, as of December 29, 2001, McLeodUSA ceased making the 50% matching contributions.

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#### **Compensation Committee Interlocks and Insider Participation**

The Compensation Committee is composed entirely of outside directors. The current members of the Compensation Committee are Thomas D. Bell, Jr., Edward D. Breen, Thomas H. Lister and Peter V. Ueberroth. During 2000 and 2001, the Compensation Committee consisted of Paul D. Rhines (January 1, 2000 through July 31, 2001), Thomas M. Collins (January 1, 2000 through October 23, 2001), Lee Liu (January 1, 2000 through May 31, 2000) and Erskine Bowles (May 31, 2000 through October 4, 2001). Mr. Liu retired from the Board of Directors on May 31, 2000. Mr. Rhines resigned from the Board of Directors effective July 31, 2001. Mr. Bowles resigned from the Board of Directors effective October 4, 2001 to seek public office as a United States Senator representing North Carolina.

During 2001 and for the six months ended June 30, 2002, McLeodUSA paid 2060 Partnership, L.P. \$349,517 and \$209,443, respectively, for the rental of office and parking spaces in Cedar Rapids, Iowa. 2001 Development Company, an Iowa corporation, is the general partner and 80% owner of 2060 Partnership, L.P. Alliant Energy and McLeodUSA own 54.56% and 3.03%, respectively of the outstanding stock of 2001 Development Company. The directors and officers of 2001 Development Company include Mr. Collins and James E. Hoffman, directors of McLeodUSA, and Clark E. McLeod, a director and executive officer of McLeodUSA until his retirement in April 2002. Mr. Lee Liu, a former Compensation Committee member, was Chairman of Alliant Energy until April 2000. Mr. Hoffman, a director of McLeodUSA, is Executive Vice President of Alliant Energy.

Mr. Collins is also a director of APAC Customer Services, Inc. ("APAC"). In March 2000, McLeodUSA entered into an agreement with APAC under which APAC provides sales, marketing and customer care services to McLeodUSA. McLeodUSA paid \$1,352,778 in 2001 and \$3,366,773 for the six months ended June 30, 2002 to APAC under this agreement. APAC paid McLeodUSA \$380,098 in 2001 and \$226,472 for the six months ended June 30, 2002 for telecommunications services. Clark E. McLeod, an executive officer and director of McLeodUSA until his retirement in April 2002, is also a director of APAC.

During 2001 and for the six months ended June 30, 2002, McLeodUSA paid \$127,698 and \$33,812, respectively, to Shuttleworth & Ingersoll, P.C., a law firm in Cedar Rapids, Iowa, for legal services rendered. McLeodUSA provides local and long distance telephone service for Shuttleworth & Ingersoll, P.C., for which McLeodUSA was paid \$40,050 in 2001 and \$20,498 for the six months ended June 30, 2002. Thomas M. Collins is Of Counsel at Shuttleworth & Ingersoll, P.C.

For a description of certain other transactions, see "Certain Relationships and Related Transactions."

#### **Employment, Confidentiality and Non-competition Contracts**

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McLeodUSA entered into executive employment agreements with Clark E. McLeod, Stephen C. Gray and Roy A. Wilkens on January 7, 2000 and with Chris A. Davis on August 1, 2001 (collectively, the "Executives"). These agreements set forth the terms and conditions for the respective employment of the Executives. The significant terms of the agreements are as follows:

*Term.* The term of each of the agreements with Messrs. McLeod, Gray and Wilkens runs until January 7, 2003. The term of the agreement with Ms. Davis runs until August 13, 2004.

*Salary and Bonus Compensation.* Each of the Executives received an initial base annual salary of \$400,000, subject to a potential increase each year based on competitive survey data. In addition, each Executive is entitled to bonus opportunities set at not less than 50% of the base annual salary. However, by mutual agreement, Mr. Wilkens' salary was reduced during 2001 to \$12,000 annually.

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*Equity Compensation.* In connection with the agreements, Mr. McLeod was granted an option to purchase 3,000,000 shares of Old Class A common stock and each of Messrs. Gray and Wilkens were granted an option to purchase 6,000,000 shares of Old Class A common stock each with an exercise price of \$17.5208 per share. Ms. Davis was granted an option to purchase 6,000,000 shares of Old Class A common stock with an exercise price of \$1.12 per share. Each option has an option exercise price equal to the fair market value of the common stock on the date of the grant which is in accordance with the McLeodUSA 1996 Employee Stock Option Plan. Each of the options granted to Messrs. McLeod, Gray and Wilkens were voluntarily cancelled in 2001. On the effective date of the Plan of Reorganization, all outstanding options were cancelled.

*Split Dollar Life Insurance.* Pursuant to Mr. McLeod's agreement, McLeodUSA has paid a portion of the premiums on split dollar life insurance premiums for the benefit of The McLeod Family 1998 Special Trust. See "Certain Relationships and Related Transactions."

*Other Benefits.* Each Executive is eligible to participate in all McLeodUSA standard benefit plans.

*Non-competition and Non-solicitation.* The Executives are bound by non-competition and non-solicitation covenants for the term of the agreements, and for an additional year in certain circumstances.

*Severance Benefits.* If an Executive terminates his or her employment for good reason or if McLeodUSA terminates such Executive's employment in breach of the agreement, the Executive is entitled to: (1) full salary through the date of termination and amounts due under any applicable compensation plan; (2) a liquidated damages payment approximately equal to the number of years (including partial years) remaining in the term of the agreement, multiplied by the Executive's salary and bonus on the date of termination; (3) full vesting of stock options granted during the term of the agreement, with such options to remain exercisable for four years; (4) continued health and related benefits for the remainder of the term of the agreement; and (5) a gross-up payment to cover excise tax payments due on the Executive's severance benefits.

*Additional Compensation and Relocation Expenses.* Ms. Davis was paid a one-time signing bonus of \$5,000,000 as compensation for loss of unvested option shares of ONI Systems Corp. ("ONI"). In addition, the agreement provided that to the extent that Ms. Davis exercises any of her vested options to purchase ONI common stock and on the earliest possible date that she can sell shares of ONI common stock, she sells any shares acquired upon such exercises and the gross sale price is less than \$24 per share, McLeodUSA shall make an additional payment to her of the difference between the sale price and \$24, for up to 162,500 shares. Ms. Davis sold the ONI common stock in accordance with her agreement and was paid \$3,186,398 for the difference between the sale price for such stock and \$24 for all 162,500 shares that she sold. Pursuant to the terms of her Agreement, McLeodUSA paid \$4.3 million to Ms. Davis to purchase her home in Los Gatos, CA, approximately \$988,000 for reimbursement of related taxes and \$118,000 for related relocation expenses.

McLeodUSA has agreements with most members of senior management, including the remaining Named Executive Officers, which govern matters of employment, non-solicitation and non-competition. These agreements typically provide that the applicable senior management

employee may not compete with McLeodUSA during the term of his or her employment and for either a one or a two-year period following a termination for cause, a resignation or a voluntary termination of employment. The agreements also provide that employees subject to the agreements may not disclose any McLeodUSA confidential information while employed by McLeodUSA or thereafter. Certain agreements provide that the employee may not solicit McLeodUSA customers or employees after leaving employment. The agreements have an indefinite term and may be terminated upon advance written notice by either party; provided, however, that the confidentiality and non-competition obligations will survive any such

termination. As partial consideration for the execution of the employment, confidentiality, and non-competition agreements, McLeodUSA granted to the employees signing such agreements options to purchase shares of Old Class A common stock at exercise prices which were based on the fair market value of the Old Class A common stock on the date of grant. Such options were granted pursuant to the McLeodUSA 1996 Employee Stock Option Plan. On the effective date of the Plan of Reorganization, all outstanding options were cancelled.

### **Change of Control Arrangements**

McLeodUSA has entered into change-of-control agreements with certain of its officers, including the Named Executive Officers who are not parties to executive employment agreements, that provide for payments and benefits in connection with specified terminations of employment after a change of control of McLeodUSA. The change-of-control agreements terminate on December 31, 2006, unless a change of control has occurred during the six months preceding December 31, 2006, in which case the agreements terminate on December 31, 2007. If an executive who is a party to a change-of-control agreement terminates employment within six months after a change of control or, if within 24 months after a change of control, the executive's employment is terminated by McLeodUSA (other than for disability, cause, death or retirement) or by the executive following a material reduction in responsibilities or compensation:

the executive will be entitled to a lump sum payment equal to between 12 and 24 times the executive's average monthly compensation during the 12 months immediately preceding the change of control or the date of termination, whichever average monthly compensation is higher;

all of the executive's outstanding options to purchase stock of McLeodUSA will become immediately exercisable in full; and

if the executive elects to continue coverage under the group health plan, McLeodUSA will continue to pay the employer portion of the premiums for such coverage for the longer of 24 months or the period of coverage provided by Section 4980B of the IRC.

An executive who is entitled to payment(s) pursuant to a change-of-control agreement is subject to a non-compete provision generally restricting the executive from competing with McLeodUSA for a two-year period after the termination of employment.

The implementation of the Plan of Reorganization caused a change of control under the agreements. Messrs. Fisher and Rings, as well as certain other officers, terminated their employment and received the benefits provided under their respective agreement.

As discussed in the section above, the executive employment agreements with Clark E. McLeod, Stephen C. Gray, Chris A. Davis and Roy A. Wilkens provide for certain payments in the event of a termination of employment. These agreements and those agreements discussed above with members of senior management also contain non-competition, non-solicitation and confidentiality covenants that are effective after employment is terminated. Mr. McLeod and Mr. Wilkens have terminated their employment and are receiving benefits pursuant to their respective agreements.

### **Compensation Committee Report on Executive Compensation**

The Compensation Committee of the Board of Directors has prepared the following report on policies with respect to the compensation of executive officers for 2001.

Decisions on compensation of executive officers are made by the Compensation Committee. The Compensation Committee also administers the McLeodUSA Incorporated 2002 Omnibus Equity Plan. No member of the Compensation Committee is an employee of McLeodUSA. The current members of the Compensation Committee are Thomas D. Bell, Jr., Edward D. Breen, Thomas H. Lister and Peter

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V. Ueberroth. During 2001, the Compensation Committee consisted of Paul D. Rhines (January 1, 2000 through July 31, 2001), Thomas M. Collins (January 1, 2000 through October 23, 2001) and Erskine Bowles (May 31, 2000 through October 4, 2001). Mr. Rhines resigned from the Board of Directors effective July 31, 2001. Mr. Bowles resigned from the Board of Directors effective October 4, 2001 to seek public office as a United States Senator representing North Carolina.

***Compensation Policies Toward Executive Officers***

The compensation policies are designed to:

attract, motivate and retain experienced and qualified executives;

increase the overall performance of McLeodUSA;

increase stockholder value; and

increase the performance of individual executives.

The Compensation Committee seeks to provide competitive salaries based upon individual performance together with annual cash bonuses awarded based on McLeodUSA's overall performance relative to corporate objectives, taking into account individual contributions, teamwork and performance levels. The Compensation Committee believes that the level of base salaries plus bonuses of executives should generally be managed to be at the midpoint of the competitive market. In addition, it is McLeodUSA's policy to grant stock options to executives in order to strengthen the alliance of interest between such executives and stockholders.

The following describes in more specific terms the elements of compensation that the Compensation Committee considers in making their determination about appropriate compensation levels, with specific reference to compensation reported for 2001:

**(a) Base Salaries**

Base salaries of executives are initially determined by evaluating the responsibilities of the position, the experience and knowledge of the individual, and the competitive marketplace for executive talent, including a comparison to base salaries for comparable positions at peer public companies in the same geographic region. Base salaries for executive officers are reviewed as appropriate by the Compensation Committee based upon, among other things, individual performance and responsibilities.

Salary adjustments for executive officers are recommended by the President and the Chief Executive Officer by evaluating the performance of each executive officer after considering new responsibilities and the previous year's performance. The Compensation Committee performs the same evaluation of the performance of Mr. Gray and Ms. Davis (the "Executives"). The Executives' employment agreements entered into on January 7, 2000 (with respect to Mr. Gray) and August 1, 2001 (with respect to Ms. Davis) are discussed in more detail above, see "Employment, Confidentiality and Non-Competition Agreements." Individual performance ratings take into account such factors as achievement of specific goals that are driven by the strategic plan and attainment of specific individual objectives. The factors impacting merit based adjustments to base salary levels are not assigned specific weights but are subject to adjustments by the Compensation Committee.

**(b) Bonuses**

Bonuses to executive officers are based on both corporate and individual performance, as measured by reference to factors which reflect objective performance criteria over which management generally has the ability to exert some degree of control. These corporate performance factors primarily consist of cash, revenue and earnings targets established in the annual budget set at the beginning of each year. Additional discretionary bonuses are occasionally awarded for exceptional performance.

Payment of cash bonuses was suspended during 2001. Other than stock options, which were granted in lieu of cash bonuses, no bonuses were awarded based on performance in 2001. On the effective date of the Plan of Reorganization, all options granted during 2001 were cancelled.

**(c) Stock Options**

A third component of executive officers' compensation involves the grant of options to purchase shares of common stock. The Compensation Committee grants stock options to executives in order to align their interests with the interests of the stockholders. Stock options are considered by the Compensation Committee to be an effective long-term incentive because the executives' gains are linked to increases in the stock value which in turn provides stockholder gains.

The Compensation Committee generally grants options to new executive officers and other key employees upon their commencement of employment with McLeodUSA and thereafter, on occasion, as determined by the Compensation Committee, based on performance. The full benefit of the options is realized upon appreciation of the stock price in future periods, thus providing an incentive to create value for McLeodUSA stockholders through appreciation of stock price. McLeodUSA believes that stock options have been helpful in attracting and retaining skilled executive personnel.

Stock option grants were made to certain executive officers in 2001 in connection with annual reviews and in lieu of a cash bonus. Certain newly hired executive officers also received stock option grants at the time of the commencement of their employment. During 2001, McLeodUSA granted stock options covering a total of approximately 24 million shares of common stock to approximately 9,000 employees, including options covering an aggregate of 6,257,500 shares of common stock, in the aggregate, to the Named Executive Officers. The per share option exercise price of such options was \$1.12 for Ms. Davis and \$6.03 for the other Named Executive Officers and from \$0.33 to \$20.46 for non-executive officer employees, which generally equaled the fair market value of a share of common stock on the respective dates of grant. These options include options granted or assumed in the conversion of options previously granted by companies acquired by McLeodUSA.

On April 16, 2002, the effective date of the Plan of Reorganization, all outstanding options were cancelled. The Plan of Reorganization provides for the establishment of a new management incentive plan, the McLeodUSA Incorporated 2002 Omnibus Equity Plan. See "APPROVAL OF THE MCLEODUSA INCORPORATED 2002 OMNIBUS EQUITY PLAN Description of the 2002 Omnibus Equity Plan."

**(d) Other**

McLeodUSA has a contributory retirement plan for its employees (including executive officers) age 21 and over with at least three months of service with McLeodUSA. The 401(k) Plan provides that each participant may contribute up to 50% (the limit was 15% for 2001 and prior years) of his or her salary (not to exceed the annual statutory limit). During 2001, McLeodUSA made matching contributions in McLeodUSA common stock to each participant's account equal to 50% of the participant's contribution up to 2% of the participant's annual compensation. In addition, McLeodUSA may make a discretionary annual match of up to another 50% of the participant's contribution up to 2% of the participant's annual compensation. Thus, the total matching contribution can be up to 4% of the participant's annual compensation. Although McLeodUSA makes such matching contributions in McLeodUSA common stock, employees are otherwise prohibited from purchasing McLeodUSA common stock with their own contributions to the 401(k) Plan. No discretionary annual match was made for 2001. In addition, as of December 29, 2001, McLeodUSA ceased making the 50% matching contributions. The Compensation Committee will reconsider the 401(k) Plan matching contribution program in the future.

***Executive Employment Agreements***

At the end of 1999, the Compensation Committee undertook a review and analysis of the existing employment and compensation arrangements with Messrs. McLeod and Gray. The Compensation Committee investigated and considered compensation, employment and stock ownership information of other telecommunications executives. As a result, the Compensation Committee approved employment agreements with Messrs. McLeod, Gray and Wilkens in January 2000. In August 2001 the Compensation Committee approved an employment agreement with Ms. Davis who joined McLeodUSA as Chief Operating and Financial Officer. See "Employment, Confidentiality and Non-Competition Agreements." The Compensation Committee manages these employment agreements and sets compensation for the Executives pursuant to these agreements.

***Chief Executive Officer Compensation***

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From January 2001 through July 2001, Messrs. McLeod and Gray served as co-Chief Executive Officers pursuant to their employment agreements. See "Employment, Confidentiality and Non-Competition Agreements." On July 31, 2001, Mr. McLeod became Chairman and Mr. Gray became President and Chief Executive Officer. The compensation of Messrs. McLeod and Gray was consistent with their employment agreements.

Mr. McLeod's compensation during the year ended December 31, 2001 included \$400,000 in base salary and \$82,350 in cash bonus (paid pursuant to the year 2000 cash bonus program). Mr. McLeod was not granted any stock options in 2001. In addition, McLeodUSA paid \$1,880,000 of premiums on split dollar life insurance policies for the benefit of the McLeod Family 1998 Special Trust in 2001 in connection with the modification of such policies. As a result of this modification, McLeodUSA was fully released from its obligations to make future payments under such policies. For additional information on this arrangement, see "Certain Relationships and Related Transactions." Mr. McLeod's salary and bonus payments for 2001 were consistent with the terms of his employment agreement.

Mr. Gray's compensation during the year ended December 31, 2001 included \$400,000 in base salary and \$82,350 in cash bonus (paid pursuant to the year 2000 cash bonus program). Mr. Gray was not granted any stock options in 2001. Mr. Gray's salary and bonus payments for 2001 were consistent with the terms of his employment agreement.

### **Compensation Deductibility Policy**

Section 162(m) of the Internal Revenue Code generally disallows a tax deduction to public corporations for compensation over \$1,000,000 paid for any fiscal year to the corporation's chief executive officer and four other most highly compensated executive officers as of the end of any fiscal year. However, the statute exempts qualifying performance-based compensation from the deduction limit if specified requirements are met. The Compensation Committee intends to structure stock option grants to executive officers who may be subject to Section 162(m) in a manner that satisfies those requirements.

The Board of Directors and the Compensation Committee reserve the authority to award non-deductible compensation in other circumstances as they deem appropriate. Further, because of ambiguities and uncertainties as to the application and interpretation of Section 162(m) and the regulations issued thereunder, no assurance can be given, notwithstanding McLeodUSA's efforts, that compensation intended by McLeodUSA to satisfy the requirements for deductibility under Section 162(m) does in fact do so.

Respectfully submitted,

Compensation Committee

Edward D. Breen, Chairman  
Thomas D. Bell, Jr.  
Thomas H. Lister  
Peter V. Ueberroth

(Following the completion of the Compensation Committee Report on Executive Compensation, Mr. McLeod retired, Chris A. Davis became Chairman and Chief Executive Officer and Mr. Gray became President.)

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### **Comparative Stock Performance**

The following chart sets forth comparative information regarding cumulative stockholder return on Old Class A common stock since the initial public offering was completed in June 1996. Total stockholder return is measured by dividing total dividends (assuming dividend reinvestment) plus share price change for a period by the share price at the beginning of the measurement period. McLeodUSA never paid a cash dividend on our Old Class A common stock. Our cumulative stockholder return based on an investment of \$100 at June 11, 1996, when the Old Class A common stock was first traded on the NASDAQ National Market, at its split-adjusted closing price of \$4.1875, is compared to the cumulative total return of the Standard & Poor's 500 Stock Index and The NASDAQ Telecommunications Stocks Index, comprised of publicly traded companies which are principally in the telecommunications business, during that same period. Because McLeodUSA has a different capital structure following the effectiveness of the Plan of Reorganization, there is no correlation between our pre-Chapter 11 and post-Chapter 11 performance.

**Comparison of Cumulative Total Returns  
Comparison of Sixty-Six Month Cumulative Total Return\*  
Among McLeodUSA Incorporated, The S&P 500 Stock Index  
and The Nasdaq Telecommunications Stocks Index**

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\$100 invested on June 11, 1996, including reinvestment of dividends, if any.

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#### **Section 16(a) Beneficial Ownership Reporting Compliance**

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires the directors, officers and greater than ten percent beneficial owners to file with the Securities and Exchange Commission initial reports of ownership of our equity securities and to file subsequent reports when there are changes in such ownership. Directors, officers and greater than ten percent beneficial owners are required by Securities and Exchange Commission regulations to furnish us with copies of all Section 16(a) reports they file.

Based on our review of these reports and on written representations from the reporting persons that no other reports were required, we believe that during the fiscal year ended December 31, 2001 our directors, officers and greater than ten percent beneficial owners complied with all applicable Section 16(a) filing requirements, except that a Form 4 for James E. Hoffman reporting the purchase of 825 shares of Old Class A common stock on May 25, 2001 was due on June 11, 2001, and was filed late on June 14, 2001.

#### **Certain Relationships and Related Transactions**

McLeodUSA has entered into various agreements with Orillion USA, Inc. (formerly InvenSys USA, Inc.) and several of its affiliates (collectively "Orillion") pursuant to which Orillion provides information technology development, programming and consulting services, and investment management services to McLeodUSA. Pursuant to these agreements, McLeodUSA paid Orillion approximately \$1,217,825 in 2001 and \$215,000 for the six months ended June 30, 2002. The payments were principally related to a \$4,000,000 license fee under a license and joint development agreement entered into in March 2000 by McLeodUSA and Orillion. Clark E. McLeod, an executive officer and director of McLeodUSA until his retirement in April 2002, was a director of Orillion USA, Inc. until his resignation in December 2000 and Roy A.

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Wilkens, a director of McLeodUSA until his resignation from the Board in May 2002, is a director of Orillion.

McLeodUSA provides paging services, customer premise equipment ("CPE"), labor and services for CPE, long distance service, 800 service and private lines to First Mid-Illinois Bancshares. First Mid-Illinois Bancshares paid McLeodUSA \$416,945 and \$243,080 for these services in 2001 and for the six months ended June 30, 2002, respectively. Richard A. Lumpkin, Margaret Lumpkin Keon and Mary Lumpkin Sparks own approximately 14.3%, 6.37% and 6.57% of the capital stock of First Mid-Illinois Bancshares, respectively. Richard A. Lumpkin, who resigned as an executive officer and director of McLeodUSA effective April 6, 2002, is a director of First Mid-Illinois Bancshares, and Mrs. Keon and Mrs. Sparks are related to Mr. Lumpkin.

McLeodUSA paid \$1,389,560 in 2001 and \$734,707 for the six months ended June 30, 2002 to lease office space from various entities in which Richard A. Lumpkin, Margaret Lumpkin Keon and Mary Lumpkin Sparks have ownership interests. Their financial interest in these transactions totaled \$838,867 in 2001 and \$431,736 for the six months ended June 30, 2002. Mr. Lumpkin was an executive officer and director of McLeodUSA until he resigned effective April 6, 2002 and Mrs. Keon and Mrs. Sparks are related to Mr. Lumpkin.

Illuminet Holdings, Inc. paid McLeodUSA \$1,986,402 in 2001 and \$1,008,134 for the six months ended June 30, 2002 for the rental of building space and for DS-1 usage and transmission facilities in the form of private leased lines. McLeodUSA paid Illuminet \$6,462,626 in 2001 and \$6,256,750 for the six months ended June 30, 2002 for database verification services and SS7 link services. Mr. Lumpkin, who resigned as an executive officer and director of McLeodUSA effective April 6, 2002, served as the Chairman of the Board of Directors of Illuminet until it was acquired by Verisign, Inc. in December 2001.

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Ameren Corporation and Central Illinois Public Service Company collectively paid McLeodUSA \$1,519,056 in 2001 and \$728,392 for the six months ended June 30, 2002 for private line services and long distance services. McLeodUSA paid Ameren and Central Illinois Public Service Company, collectively, \$1,233,168 and \$587,712 for electric utility services in 2001 and for the six months ended June 30, 2002, respectively. Richard A. Lumpkin, who resigned as an executive officer and director of McLeodUSA effective April 6, 2002, is a director of Ameren Corporation, the parent company of Central Illinois Public Service Company.

Chris A. Davis receives an annual salary of \$500,000 for providing advice and consulting services to Forstmann Little as a special limited partner thereof. Ms. Davis has the right to invest in Forstmann Little portfolio investments from time to time. Ms. Davis has informed McLeodUSA that she did not invest in Forstmann Little's investment in McLeodUSA in connection with the restructuring. Ms. Davis has agreed to provide her advice related to the investment activities of the Forstmann Little partnerships in a manner that does not interfere with the performance of her duties with McLeodUSA.

McLeodUSA is a party to an agreement with Alliant Energy pursuant to which Alliant Energy grants McLeodUSA access to certain of Alliant Energy's towers, rights-of-way, conduits and poles in exchange for capacity on the McLeodUSA communications network. McLeodUSA paid \$1,654,096 and \$598,663 to Alliant during 2001 and for the six months ended June 30, 2002, respectively, primarily for utilities. Alliant Energy paid McLeodUSA \$404,937 for the six months ended June 30, 2002 for telecommunications services. James E. Hoffman (Executive Vice President Business Development of Alliant Energy) is, and Mr. Lee Liu (a former director of McLeodUSA and former Chairman of Alliant Energy) was from 1993 to 2000, a director of McLeodUSA.

In December 2001, Ruffalo, Cody & Associates, a McLeodUSA subsidiary, sold substantially all of its assets to RCNEWCO, an Iowa Corporation. Clark E. McLeod, Chairman and director of McLeodUSA until his retirement in April 2002, is an indirect investor in RCNEWCO, with an ownership interest of approximately 7%.

During 2001, McLeodUSA paid City Signal Communications \$334,908 for network construction services. Peter H.O. Claudy, a director of McLeodUSA until his resignation in May 2002, is a director for City Signal Communications.

In 2001, McLeodUSA paid \$2,811,417 to The Management Network Group, Inc. ("TMNG") for telecommunications consulting services with TMNG. Roy A. Wilkens, who resigned as a director of McLeodUSA in May 2002, is a director of TMNG.

McLeodUSA paid Williams Communication Group, a provider of services and products to communications companies, \$1,282,439 in 2001 and \$589,725 for the six months ended June 30, 2002. Roy A. Wilkens was a director of Williams Communication Group before he resigned that position in December 2000.

McLeodUSA paid Image Media Group, Inc., a promotional products supplier, \$156,916 in 2001. Arthur L. Christoffersen, an executive officer of McLeodUSA until April 2002, is a director of Image Media Group.



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During 2001 and for the six months ended June 30, 2002, McLeodUSA paid Motorola \$172,766 and \$125,720, respectively, for paging services and commissions on certain telecommunications services McLeodUSA provides. Edward D. Breen, a director of McLeodUSA, was Executive Vice President of Motorola and President of its Network Sector during 2001 and thereafter was the President and Chief Operating Officer of Motorola until July 2002.

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During 2001, McLeodUSA paid Hilton Hotels Corporation approximately \$120,917 for room rental, hotel services and commissions on certain telecommunications services McLeodUSA provides. Peter V. Ueberroth, a director of McLeodUSA, serves on the board of Hilton Hotels Corporation.

McLeodUSA paid Bank of America \$4 million in arranger fees upon the closing of the \$110 million exit financing facility from a group of lenders arranged by JPMorgan, Bank of America and Citibank (the "Exit Facility"). McLeodUSA paid Bank of America \$62,373 during the six months ended June 30, 2002 primarily for commissions on certain telecommunications services McLeodUSA provides. Bank of America is also a lender under the Exit Facility. Peter V. Ueberroth, a director of McLeodUSA, serves on the board of Bank of America.

During 2001, Community Health Systems paid McLeodUSA \$145,975 for private line and long distance services. Theodore J. Forstmann, Thomas H. Lister and Dale F. Frey, directors of McLeodUSA, serve on the board of Community Health Systems.

During 2001 and for the six months ended June 30, 2002, McLeodUSA paid \$109,984 and \$69,143, respectively, to Cousins Properties Incorporated for real estate rental. Thomas D. Bell, Jr., a director of McLeodUSA, is President and CEO, and a director of Cousins Properties Incorporated.

During 2001, McLeodUSA paid \$16,580,324 to Credit Suisse Group for services rendered in 2000 in connection with McLeodUSA's acquisition of Splitrock Services, Inc. During 2002, McLeodUSA paid \$3,584,363 to Credit Suisse Group for services rendered in connection with the sale of McLeodUSA's publishing business. Thomas D. Bell, Jr. is a director of Credit Suisse Group.

During 2001 and 2002, McLeodUSA entered into indemnity agreements with certain of its officers and directors to provide protection against personal liability in order to insure and enhance those individual's continued service to McLeodUSA in an effective manner. The agreements provide for the effective indemnification of and the advancing of expenses to those individuals to the fullest extent (whether partial or complete) permitted by law and as set forth in the agreements, and, to the extent insurance is maintained, for the continued coverage of those individuals under McLeodUSA's director and officer liability insurance policies.

The ownership of a jet aircraft worth approximately \$6 million is held 95.2% by McLeodUSA, and 2.4% each by Messrs. Gray and Lumpkin. McLeodUSA and Messrs. Gray and Lumpkin are parties to a Joint Ownership Agreement by which they have agreed to share the operational expenses of the aircraft in proportion to their respective ownership interest in the aircraft. Mr. Gray is a director and executive officer of McLeodUSA, and Mr. Lumpkin was a director and executive officer of McLeodUSA until his resignation effective April 6, 2002.

In February 2000, McLeodUSA and C&M Consulting, L.L.C. ("C&M") jointly purchased a jet aircraft for a total price of approximately \$39.5 million. McLeodUSA and C&M are parties to a Joint Ownership Agreement in which they have agreed to share operational expenses associated with the aircraft, some expenses in proportion to their ownership interests (25% by McLeodUSA and 75% by C&M) and others in proportion to the actual usage of the aircraft. Clark E. McLeod and his wife, Mary E. McLeod, are the members of C&M. At December 31, 2001, Mr. McLeod owed McLeodUSA approximately \$1.4 million for expenses related to the jointly held aircraft. In March 2002, McLeodUSA and C&M sold the aircraft, the proceeds were dispersed in proportion to the ownership interests and the receivable was paid.

In December 1998, McLeodUSA entered into a split dollar agreement for life insurance policies on the joint lives of Clark and Mary McLeod. The McLeod Family 1998 Special Trust is sole owner and beneficiary of each policy. The McLeod Family 1998 Special Trust agreed to assign the policies to McLeodUSA as collateral for the payment by McLeodUSA of the premiums for these policies. The aggregate face amount of the policies was \$113,000,000. McLeodUSA agreed with Clark and Mary

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McLeod that one of the principal reasons for entering into the agreement was to avoid any need for their heirs to liquidate their holdings of Old Class A common stock at or soon after the death of one or both of them. Clark and Mary McLeod agreed to restrictions on their ability to sell or

otherwise dispose of their shares of Old Class A common stock. By the terms of the split dollar agreement, McLeodUSA's obligation to make premium payments would terminate upon the twentieth anniversary, or earlier termination, of the agreement. Upon termination prior to the death of the survivor of Clark and Mary McLeod, McLeodUSA was entitled to receive from the trustees of the McLeod Family 1998 Special Trust an amount equal to the aggregate total premiums McLeodUSA paid.

In July 2001, McLeodUSA, for consideration received, agreed to modify the terms of the split dollar agreement to eliminate its ability to unilaterally cancel the agreement. As of December 2001, McLeodUSA made annual premium payments pursuant to the agreement of \$1.88 million for each of 1998, 1999 and 2000. As of December 2001, the life insurance policies held by the trustees had a net cash surrender value of \$2.7 million.

In January 2002, McLeodUSA and the trustees entered into a modification and restatement of the split dollar agreement pursuant to which the trustees made a payment to McLeodUSA in the amount of \$2.7 million in exchange for McLeodUSA's release of its collateral assignments on the existing policies and for McLeodUSA's agreement to make a single further premium payment of \$1.88 million (the payment otherwise due in December 2001 under the split dollar agreement, as modified) to acquire additional insurance on the lives of Clark and Mary McLeod. As a result of this modification and restatement, McLeodUSA was fully released from its obligations to make future payments under such policies. The additional life insurance policy is owned by McLeodUSA, subject to a split dollar endorsement in favor of the trustees. Pursuant to this endorsement, at any time after December 31, 2003, the trustees have the option to purchase this policy from McLeodUSA for the policy's then net cash surrender value. Upon the trustees' exercise of such option, the restrictions on Clark and Mary McLeod's Old Class A common stock contained in the split dollar agreement will terminate.

McLeodUSA paid CommScope, Inc. \$287,970 for equipment during 2001. Edward D. Breen, a director of McLeodUSA, is a director of CommScope, Inc.

Forstmann Little & Co. has a significant equity interest in both McLeodUSA and XO Communications, Inc. ("XO"). XO purchases interconnection and facilities based telecommunications services from McLeodUSA. In addition, during 2001, XO acquired certain unlit metro network capacity from McLeodUSA. The payments received for such services and capacity totaled \$8,554,050 for 2001 and \$548,648 for the six months ended June 30, 2002. McLeodUSA purchased certain unlit metro network capacity and other telecommunications services from XO during 2001 and the six months ended June 30, 2002 for \$8,480,513 and \$315,066, respectively.

In March 1996, the Board of Directors adopted a policy requiring that any material transactions between McLeodUSA and persons or entities affiliated with officers, directors or principal stockholders of McLeodUSA be on terms no less favorable to McLeodUSA than reasonably could have been obtained in arms' length transactions with independent third parties or be approved by a majority of disinterested directors.

Theodore J. Forstmann is a senior partner and Thomas H. Lister is a general partner of Forstmann Little & Co. Funds affiliated with Forstmann Little are parties to several agreements related to our restructuring. In addition, Dale F. Frey is an investor in Forstmann Little and serves on the Forstmann Little advisory board.

For a description of certain other transactions, see " Compensation Committee Interlocks and Insider Participation."

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**RATIFICATION OF THE APPOINTMENT  
OF THE COMPANY'S INDEPENDENT PUBLIC ACCOUNTANTS  
FOR THE 2002 FISCAL YEAR  
(Proposal 2)**

At the recommendation of the Audit Committee of the Board of Directors, effective April 25, 2002, the Board of Directors appointed the firm of Deloitte & Touche LLP as independent public accountants for the fiscal year ending December 31, 2002.

Arthur Andersen LLP was our principal independent public accountants for the fiscal year ending December 31, 2001 and the preceding four years. On April 24, 2002, we determined to dismiss Arthur Andersen LLP, effective on such date, and on April 25, 2002, we appointed Deloitte & Touche LLP as our new independent auditors, effective on such date. Our Board of Directors approved the decision not to renew the engagement of Arthur Andersen LLP and to retain Deloitte & Touche LLP upon the recommendation of our Audit Committee. The decision was based on discussions with large accounting firms and reflected our Audit Committee's judgment as to which firm was best suited to deliver external audits to us in light of relevant factors such as the firm's depth of experience, breadth of resources, commitment to provide exceptional service, ability to handle transition issues and location of key personnel.

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Stockholder ratification of Proposal 2 is not required by the Bylaws or otherwise. However, the Board of Directors is submitting Proposal 2 to the stockholders for ratification as a matter of good corporate practice. If the stockholders fail to ratify Proposal 2, the Board of Directors will reconsider whether or not to retain Deloitte & Touche LLP. Even if Proposal 2 is ratified, the Board of Directors in its discretion may direct the appointment of a different independent accountant at any time during the year if the Board of Directors determines that such a change would be in the best interests of McLeodUSA and its stockholders.

It is expected that representatives of Deloitte & Touche LLP will be present at the Annual Meeting and will have the opportunity to make a statement if they so desire and will be available to respond to appropriate questions.

The audit reports of Arthur Andersen LLP on our financial statements as of and for the fiscal years ended December 31, 2000 and December 31, 2001 (as presented in the 2001 Annual Report on Form 10-K/A filed April 19, 2002) did not contain any adverse opinion or disclaimer of opinion, nor were they qualified or modified as to uncertainty, audit scope, or accounting principles.

During our two fiscal years ended December 31, 2001 and the subsequent period through April 24, 2002, there were no disagreements between us and Arthur Andersen LLP on any matter of accounting principles or practices, financial statement disclosure, or auditing scope or procedures, which disagreements if not resolved to Arthur Andersen LLP's satisfaction would have caused them to make reference to the subject matter of the disagreement in connection with their reports.

None of the reportable events described under Item 304(a)(1)(v) of Regulation S-K occurred within our two fiscal years ended December 31, 2001 and the subsequent period through April 24, 2002.

During our two fiscal years ended December 31, 2001 and the subsequent period through April 24, 2002, we did not consult with Deloitte & Touche LLP regarding any of the matters or events set forth in Item 304(a)(2)(i) and (ii) of Regulation S-K.

During 2001, we paid the following fees to Arthur Andersen LLP:

- 1) *Audit Fees:* annual audit and quarterly reviews, \$611,100;
- 2) *Financial Information Systems Design and Implementation Fees:* \$255,000; and
- 3) *All Other Fees:* \$899,361. All other fees principally included SEC filings, tax compliance, tax consulting, and other services.

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The Audit Committee considered whether the provision of services covered by Financial Information Systems Design and Implementation Fees and All Other Fees is compatible with maintaining the independence of Arthur Andersen LLP.

The affirmative vote of a majority of the voting rights represented at the Annual Meeting is required to approve Proposal 2.

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE "FOR" PROPOSAL 2.**

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### **APPROVAL OF THE McLeodUSA Incorporated 2002 Omnibus Equity Plan (Proposal 3)**

The Board of Directors has approved the McLeodUSA Incorporated 2002 Omnibus Equity Plan (the "Omnibus Plan"). A copy of the Omnibus Plan is included as Appendix A to this Proxy Statement.

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Our Board of Directors believes that the maintenance of the Omnibus Plan is necessary to meet our objectives of attracting, retaining and compensating key employees.

### Description of the 2002 Omnibus Equity Plan

A description of the provisions of the Omnibus Plan is set forth below. This summary is qualified in its entirety by the provisions of the Omnibus Plan, a copy of which is attached as Appendix A to this proxy statement.

*Administration.* The Omnibus Plan is administered by the full Board of Directors of McLeodUSA or a committee thereof (the "Committee"). Subject to the terms of the Omnibus Plan, the Committee may select participants to receive awards, determine the types of awards and terms and conditions of awards, and interpret provisions of the Omnibus Plan.

*Common Stock.* The McLeodUSA common stock issued or to be issued under the Omnibus Plan consists of treasury shares or authorized but unissued shares. If any award expires or is terminated for any reason prior to exercise in full, the shares of stock that were subject to the expired or terminated portion of such award will be available for future awards granted under the Omnibus Plan. A total of 65,173,797 shares of McLeodUSA common stock are reserved for issuance under the Omnibus Plan. The market value of a share of common stock was \$0.44 as of August 1, 2002, based on the last trade price listed in the Wall Street Journal for such date.

*Eligibility.* Awards may be made under the Omnibus Plan to officers and key employees of McLeodUSA or any of our affiliates, to non-employee directors, and to other non-employee service providers and consultants whose participation in the Omnibus Plan is determined to be in the best interests of McLeodUSA by the Committee. As of July 31, 2002, there were approximately 4,700 employees of McLeodUSA and its subsidiaries, 12 non-employee directors and many other non-employee service providers and consultants who were eligible to participate in the Omnibus Plan.

*Amendment or Termination of the Omnibus Plan.* The Board of Directors may terminate or amend the Omnibus Plan at any time and for any reason. Unless extended, the Omnibus Plan will terminate on April 16, 2012. Amendments to the Omnibus Plan will be submitted for stockholder approval to the extent required by the Internal Revenue Code or other applicable laws.

*Awards.* The Omnibus Plan permits the granting of options (both incentive stock options and options which do not qualify as incentive stock options, known as nonqualified stock options), shares of restricted common stock, phantom stock (the right to receive cash shares or other property the value of which is tied to the fair market value of a share of common stock), stock bonuses and other awards.

*Transferability.* In general, awards granted under the Omnibus Plan may not be sold, transferred, pledged or assigned other than by will or under applicable laws of descent and distribution. The Omnibus Plan permits limited transfers of nonqualified stock options for the benefit of immediate family members to help with estate planning concerns.

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*Effect of Certain Corporate Transactions.* Unless otherwise determined by the Committee, upon the occurrence of a change or exchange of the McLeodUSA common stock for other property pursuant to a recapitalization, reclassification, merger, consolidation, combination or other similar transaction, (1) each option will, subject to certain adjustments, become exercisable for the number and/or kind of property into which the shares of common stock subject to the option would have been exercisable in full prior to such transaction and (2) each award that is not an option and that is not automatically changed in connection with the transaction will represent the number and/or kind of property into which the number shares of common stock covered by the award would have been changed or exchanged had they been held by a shareholder of McLeodUSA.

*Adjustments for Stock Dividends and Similar Events.* The Committee will make appropriate adjustments in outstanding awards and the number of shares available for issuance under the Omnibus Plan, including the individual limitations on awards, to reflect stock dividends, stock splits and other similar events.

### Grants Under the Omnibus Plan

The table below shows, as to the Named Executive Officers (as defined in "EXECUTIVE COMPENSATION AND OTHER INFORMATION" above) and the other individuals and groups indicated, the number of shares of McLeodUSA common stock subject to option grants made in the aggregate under the Omnibus Plan from April 18, 2002 through July 31, 2002, together with the weighted average exercise price payable per share. No awards other than stock options were granted in that period.

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Underlying Exercise Price Name and Position	Options Granted (#)	Per Share (\$)
Chris A. Davis Chairman and Chief Executive Officer	7,000,000	\$ 1.11
Stephen C. Gray President	4,500,000	\$ 1.11
G. Kenneth Burckhardt Executive Vice President and Chief Financial Officer	2,500,000	\$ 1.11
All current executive officers as a group	14,000,000	\$ 1.11
All current non-employee directors as a group	5,025,000	\$ 1.11
All employees, including current officers who are not executive officers, as a group	32,749,050	\$ 1.11

As of July 31, 2002, 65,173,797 shares of McLeodUSA common stock will have been available for issuance assuming stockholder approval of this Proposal, of which 37,774,050 options have been granted, and 27,399,747 shares remained available for future issuance under the Omnibus Plan.

**New Benefits Under the Omnibus Plan**

Because participation in, and the types of options awarded under, the Omnibus Plan are subject to the discretion of the Committee, the benefits or amounts that will be received by any participant or groups of participants if the adoption of the Omnibus Plan is approved are not currently determinable.

**Federal Income Tax Consequences**

The following discussion is a brief summary of the principal United States Federal income tax consequences under current Federal income tax laws relating to options under the Omnibus Plan. This summary is not intended to be exhaustive and, among other things, does not describe state, local or foreign income and other tax consequences.

*Section 162(m) of the Code.* Section 162(m) of the Code limits publicly-held companies such as McLeodUSA to an annual deduction for federal income tax purposes of \$1,000,000 for compensation paid to their chief executive officer and the four other highest compensated executive officers determined at the end of each year. However, performance-based compensation is excluded from this limitation. The Omnibus Plan is designed to permit the Committee to grant options that qualify as performance-based for purposes of satisfying the conditions of Section 162(m).

Compensation attributable to stock options will generally qualify as performance-based compensation if:

the grant is made by a committee of non-employee directors;

the plan under which the option is granted states the maximum number of shares with respect to which options may be granted during a specified period to an employee; and

under the terms of the option, the amount of compensation is based solely on an increase in the value of the stock after the date of grant.

The maximum number of shares of McLeodUSA common stock subject to awards that can be awarded under the Omnibus Plan, as amended, to any person in a calendar year is 50,000,000.

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*Incentive Stock Options.* The grant of an option will not be a taxable event for the optionee or for us. An optionee will not recognize taxable income upon exercise of an incentive stock option (except that the alternative minimum tax may apply), and any gain realized upon a disposition of our common stock received pursuant to the exercise of an incentive stock option will be taxed as long-term capital gain if the optionee holds the shares for at least two years after the date of grant and for one year after the date of exercise (the "holding period requirement"). We will not be entitled to any compensation expense deduction with respect to the exercise of an incentive stock option, except as discussed below. For the exercise of an option to qualify for the foregoing tax treatment, the optionee generally must be our employee or an employee of our subsidiary from the date the option is granted through a date within three months before the date of exercise of the option. If all of the foregoing requirements are met except the holding period requirement mentioned above, the optionee will recognize ordinary income upon the disposition of common stock in an amount generally equal to the excess of the fair market value of our common stock at the time the option was exercised over the option exercise price (but not in excess of the gain realized on the sale). The balance of the realized gain, if any, will be capital gain. We will generally be allowed a compensation expense deduction to the extent the optionee recognizes ordinary income.

*Non-Qualified Options.* The grant of an option will not be a taxable event for the optionee. Upon exercising a non-qualified option, an optionee will recognize ordinary income in an amount equal to the difference between the exercise price and the fair market value of our common stock on the date of exercise. Upon a subsequent sale or exchange of shares acquired pursuant to the exercise of a non-qualified option, the optionee will have taxable gain or loss, measured by the difference between the amount realized on the disposition and the tax basis of the shares (generally, the amount paid for the shares plus the amount treated as ordinary income at the time the option was exercised). We will

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generally be entitled to a business expense deduction in the same amount and generally at the same time as the optionee recognizes ordinary income. An optionee who has transferred a non-qualified stock option to a spouse, child, grandchild, parent or sibling by gift will realize taxable income at the time the option is exercised by the family member. The optionee will be subject to withholding of income and employment taxes at that time. The family member's tax basis in the shares will be the fair market value of the shares on the date the option is exercised. The transfer of vested non-qualified stock options will be treated as a completed gift for gift and estate tax purposes. Once the gift is completed, neither the transferred options nor the shares acquired on exercise of the transferred options will be includable in the optionee's estate for estate tax purposes.

### Equity Compensation Plan Information

The following table presents certain information about McLeodUSA's equity compensation plans as of the end of the McLeodUSA's most recently completed fiscal year. In accordance with SEC rules, the table does not reflect the impact of the proposed adoption of the Omnibus Plan.

Plan Category	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted-average exercise price of outstanding options, warrants and rights	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	105,342,022	\$ 8.60	110,112,364
Equity compensation plans not approved by security holders	0	0	0
<b>Total</b>	<b>105,342,022</b>	<b>\$ 8.60</b>	<b>110,112,364</b>

On the effective date of the Plan of Reorganization, all options granted during 2001 pursuant to McLeodUSA's equity compensation plans reflected in the above table were cancelled.

The affirmative vote of a majority of the voting rights represented at the Annual Meeting is required to approve Proposal 3.

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE "FOR" PROPOSAL 3.**

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### Report of the Audit Committee

The Audit Committee of the Board of Directors has prepared the following report for 2001.

To the Board of Directors of McLeodUSA Incorporated:

The Audit Committee has reviewed and discussed with management McLeodUSA's audited financial statements as of and for the year ended December 31, 2001.

The Audit Committee has discussed with Arthur Andersen LLP the matters required to be discussed by Statement on Auditing Standards No. 61, *Communication with Audit Committees*, as amended, by the Auditing Standards Board of the American Institute of Certified Public Accountants.

The Audit Committee has received and reviewed the written disclosures and the letter from Arthur Andersen LLP required by Independence Standard No. 1, *Independence Discussions with Audit Committees*, as amended, by the Independence Standards Board, and have discussed with the auditors the auditors' independence.

Based on the reviews and discussions referred to above, the Audit Committee recommends to the Board of Directors that the audited financial statements referred to above be included in the McLeodUSA Annual Report on Form 10-K for the year ended December 31, 2001 for filing with the Securities and Exchange Commission.

Respectfully submitted,  
Audit Committee  
Dale F. Frey, Chairman  
Thomas M. Collins

(Farid Suleman was appointed to the Audit Committee following the completion of the Report of the Audit Committee.)

### STOCK OWNERSHIP BY MANAGEMENT AND MORE THAN 5% STOCKHOLDERS

The following beneficial ownership table sets forth information regarding beneficial ownership of McLeodUSA voting stock as of July 31, 2002 by:

each director and director nominee;

each Named Executive Officer;

each other person known by McLeodUSA to beneficially own more than 5% of a class of stock of McLeodUSA; and

all executive officers and directors as a group.

Under the Exchange Act, a person is deemed to be a "beneficial owner" of a security if he or she has or shares the power to vote or direct the voting of such security or the power to dispose or direct the disposition of such security. A person is also deemed to be a beneficial owner of any securities of which that person has the right to acquire beneficial ownership within 60 days. More than one person may be deemed to be a beneficial owner of the same securities. The percentage ownership of each stockholder is calculated based on the total number of outstanding shares of the applicable class of stock as of July 31, 2002 plus those shares of stock that such stockholder has the right to acquire within 60 days. Consequently, the denominator for calculating such percentage may be different for each stockholder.

With respect to directors, director nominees and executive officers, the table is based upon information supplied by such persons. The information regarding more than 5% stockholders is based

on the most recent Schedule 13D or 13G filed with the SEC on behalf of such persons or other information made available to us.

Unless otherwise indicated in the footnotes to the table, each of the stockholders listed has sole voting and dispositive power with respect to the shares shown as beneficially owned.

Name of Beneficial Owner	Class A Common			Class B Common		Class C Common		Series A Preferred		Series B Preferred	
	Number of Option Shares <sup>1</sup>	Number of Shares and Option Shares	Percent of Class	Number of Shares	Percent of Class	Number of Shares	Percent of Class	Number of Shares	Percent of Class	Number of Shares	Percent of Class
Chris A. Davis	3,500,000	3,500,000	2.11								
Stephen C. Gray	1,125,000	1,230,047	*								
G. Kenneth Burckhardt	625,000	625,000	*								
Thomas D. Bell, Jr.	100,000	100,000	*								
Jeffrey D. Benjamin	75,000	75,000	*								
Edward D. Breen	125,000	125,000	*								
Thomas M. Collins	100,000	150,010	*								
Theodore J. Forstmann (2)	181,250	210,118,119	70.37	78,203,135	100	35,546,879	100			10	100
Dale F. Frey	125,000	125,000	*								
James E. Hoffman	75,000	75,242	*								
Jeong H. Kim	0	0	0								
Thomas H. Lister (3)	125,000	210,061,869	70.36	78,203,135	100	35,546,879	100			10	100
Farid Suleman	0	0	0								
Peter V. Ueberroth	100,000	100,000	*								
Juan Villalonga	0	0	0								
Clark E. McLeod	500,000	2,093,635	1.2								
Roy A. Wilkens	300,000	369,253	*								
Arthur L. Christoffersen	0	5,858	*								
Randall Rings	0	705	*								
Blake O. Fisher, Jr.	0	31,272	*								
Forstmann Little & Co. Subordinated Debt & Equity Management Buyout Partnership VI, L.P.(4)			13**	24,383,737	31						
Forstmann Little & Co. Subordinated Debt & Equity Management Buyout Partnership VII, L.P.(4)			24.9**	53,819,398	69						
Forstmann Little & Co. Equity Partnership V, L.P.(4)			17.9**			35,546,879	100				
Forstmann Little & Co. Subordinated Debt & Equity Management Buyout Partnership VIII, L.P.(5)		36,070,071	21.1***							3.75	37.5
Forstmann Little & Co. Equity Partnership VII, L.P.(6)		60,116,784	34.1****							6.25	62.5
Directors and executive officers as a group (15 persons)	6,256,250	6,411,548	3.8								

\*



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Less than one percent

\*\*

Percentages of Class A Common Stock based on 162,499,986 shares of Class A Common Stock outstanding as of July 31, 2002, including 18,000,000 shares of Class A Common Stock held in the disputed claims reserve pursuant to the Plan of Reorganization, not assuming the conversion of the Class B Common Stock and Class C Common Stock held by other stockholders.

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Percentage of Class A Common Stock based on 170,809,645 shares of Class A Common Stock outstanding as of July 31, 2002, including 18,000,000 shares of Class A Common Stock held in the disputed claims reserve pursuant to the Plan of Reorganization, not assuming the conversion of the Class B Common Stock and Class C Common Stock, but assuming the exercise of warrants held by such beneficial owner but not the exercise of any other warrants.

\*\*\*\*

Percentage of Class A Common Stock based on 176,349,418 shares of Class A Common Stock outstanding as of July 31, 2002 including 18,000,000 shares of Class A Common Stock held in the disputed claims reserve pursuant to the Plan of Reorganization, not assuming the conversion of the Class B Common Stock and Class C Common Stock, but assuming the exercise of warrants held by such beneficial owner but not the exercise of any other warrants.

(1)

Includes shares of Class A Common Stock that the individuals named in the table have the right to acquire within 60 days from July 31, 2002 upon exercise of options.

(2)

See notes 4 through 6. Percentage of Class A Common Stock ownership based on 298,590,341 shares of Class A Common Stock outstanding, assuming the conversion of all of the outstanding shares of Class B Common Stock and Class C Common Stock into shares of Class A Common Stock, the exercise of warrants held by certain Forstmann Little funds for 22,159,091 shares of Class A Common Stock and the exercise of Mr. Forstmann's options, but not assuming the conversion of the Series A Preferred Stock into shares of Class A Common Stock or the exercise of any other warrants.

(3)

See notes 4 through 6. Percentage of Class A Common Stock ownership based on 298,534,091 shares of Class A Common outstanding, assuming the conversion of all of the outstanding shares of Class B Common Stock and Class C Common Stock into shares of Class A Common Stock, the exercise of warrants held by certain Forstmann Little funds for 22,159,091 shares of Class A Common Stock and the exercise of Mr. Lister's options, but not assuming the conversion of the Series A Preferred Stock into shares of Class A Common Stock or the exercise of any other warrants.

(4)

The Class B Common Stock and the Class C Common Stock, in the aggregate, are convertible into 113,750,014 shares of McLeodUSA's Class A Common Stock. However, the number of shares of Class A Common Stock into which each of the Class B Common Stock and the Class C Common Stock is convertible is not calculable at the present time. The respective portions of the 113,750,014 shares of Class A Common Stock into which the shares of Class B Common Stock and the shares of Class C Common Stock are convertible are calculated in accordance with a formula set forth in the Certificate of Incorporation, which formula is dependent on the fair market value of a share of Class A Common Stock at the time of conversion and the timing of the conversion.

FLC XXIX Partnership, L.P. is the general partner of Forstmann Little & Co. Subordinated Debt & Equity Management Buyout Partnership VI, L.P., the direct owner of 24,383,737 shares of Class B Common Stock. Theodore J. Forstmann, Sandra J. Horbach, Thomas H. Lister, Winston W. Hutchins, Jamie C. Nicholls, and Gordon Holmes, are the general partners of FLC XXIX. FLC XXXIII Partnership, L.P. is the general partner of Forstmann Little & Co. Subordinated Debt & Equity Management Buyout Partnership VII, L.P., the direct owner of 53,819,398 shares of Class B Common Stock. Theodore J. Forstmann, Sandra J. Horbach, Thomas H. Lister, Winston W. Hutchins, Jamie C. Nicholls and Gordon Holmes are the general partners of FLC XXXIII. FLC XXX Partnership, L.P. is the general partner of Forstmann Little & Co. Equity Partnership V, L.P., the direct owner of 35,546,879 shares of Class C Common Stock. Theodore J. Forstmann, Sandra J. Horbach, Thomas H. Lister and Winston W. Hutchins are the general partners of FLC XXX. The address for each of Forstmann Little & Co. Subordinated Debt & Equity Management Buyout Partnership VI, L.P., Forstmann Little & Co. Subordinated Debt & Equity Management Buyout Partnership VII, L.P. and Forstmann Little & Co. Equity Partnership V, L.P. is c/o Forstmann Little & Co., 767 Fifth Street New York, NY 10153.

(5)

FLC XXXIII Partnership, L.P. is the general partner of Forstmann Little & Co. Subordinated Debt & Equity Management Buyout Partnership VIII, L.P., the direct owner of 27,760,412 shares of Class A Common Stock and warrants to purchase 8,309,659 shares of Class A Common Stock, which are currently exercisable. Theodore J. Forstmann, Sandra J. Horbach, Thomas H. Lister, Winston W. Hutchins, Jamie C. Nicholls and Gordon Holmes are the general partners of FLC XXXIII. The address of Forstmann Little & Co. Subordinated Debt & Equity Management Buyout Partnership VIII, L.P. is c/o Forstmann Little & Co., 767 Fifth Street New York, NY 10153.

(6)

FLC XXXII Partnership, L.P. is the general partner of Forstmann Little & Co. Equity Partnership VII, L.P., the direct owner of 46,267,352 shares of Class A Common Stock and warrants to purchase 13,849,432 shares of Class A Common Stock, which are currently exercisable. Theodore J. Forstmann, Sandra J. Horbach, Thomas H. Lister, Winston W. Hutchins, Jamie C. Nicholls and Gordon Holmes are the general partners of FLC XXXII. The address of Forstmann Little & Co. Equity Partnership VII, L.P. is c/o Forstmann Little & Co., 767 Fifth Street New York, NY 10153.

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**SUBMISSION OF STOCKHOLDER PROPOSALS  
FOR THE 2003 ANNUAL MEETING**

Any proposal or proposals by a stockholder intended to be included in the proxy statement and form of proxy relating to the 2003 annual meeting of stockholders must be received by us no later than April 11, 2003 pursuant to the proxy solicitation rules of the SEC, provided, however, that if the date of the 2003 annual meeting is changed by more than 30 days from the date of the 2002 annual meeting, then the deadline will be a reasonable time before McLeodUSA begins to print and mail the 2003 proxy materials. Your proposals should be sent by certified mail, return receipt requested, to Corporate Secretary, McLeodUSA Incorporated, 6400 C Street SW, P.O. Box 3177, Cedar Rapids, Iowa 52406-3177. Nothing in this paragraph shall be deemed to require us to include in our proxy statement and proxy relating to the 2003 annual meeting of stockholders any stockholder proposal which may be omitted from the proxy materials pursuant to applicable regulations of the SEC in effect at the time such proposal is received.

Notice of any proposal or proposals by a stockholder that is not submitted for inclusion in next year's proxy statement but is instead presented directly at the 2003 annual meeting of stockholders must be received by us no earlier than June 15, 2003 and no later than July 15, 2003, provided, however, that if the date of the 2003 annual meeting is changed by more than 30 days from the date of the 2002 annual meeting, then the deadline will be the close of business on the tenth day following the date on which notice of the date of the annual meeting was mailed or public disclosure of the date of the annual meeting was made, whichever first occurs. Notices of intention to present proposals at the 2003 annual meeting should be addressed to Corporate Secretary, McLeodUSA Incorporated, 6400 C Street SW, P.O. Box 3177, Cedar Rapids, Iowa 52406-3177.

**OTHER MATTERS THAT MAY COME BEFORE THIS YEAR'S ANNUAL MEETING**

Our Board of Directors does not know of any other matters to be presented for a vote at the Annual Meeting. If, however, any other matter should properly come before the Annual Meeting or any adjournment thereof, the persons named in the accompanying proxy will vote such proxy in accordance with their best judgment.

By Order of the Board of Directors

/s/ CHRIS A. DAVIS

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Chris A. Davis  
*Chairman and Chief Executive Officer*

Cedar Rapids, Iowa  
August 7, 2002

**A copy of the Annual Report to Stockholders for the fiscal year ended December 31, 2001 accompanies this Proxy Statement and it includes an Annual Report on Form 10-K/A for the fiscal year ended December 31, 2001 that we filed with the SEC. Stockholders may obtain, free of charge, an additional copy of the Annual Report on Form 10-K/A by writing to McLeodUSA Incorporated, 6400 C Street SW, P.O. Box 3177, Cedar Rapids, Iowa 52406-3177, Attention: Corporate Secretary. McLeodUSA will provide copies of the exhibits to the Form 10-K upon payment of a reasonable fee.**

**2002 OMNIBUS EQUITY PLAN**

**1. Purpose; Establishment.**

The McLeodUSA Incorporated 2002 Omnibus Equity Plan (the "Plan") is intended to promote the interests of the Company and its shareholders by providing officers, other employees of the Company (including directors who are also employees of the Company) and nonemployee directors with appropriate incentives and rewards to encourage them to enter into and continue in the employ or service of the Company and to acquire a proprietary interest in the long-term success of the Company; and to reward the performance of individual officers, other employees, consultants and nonemployee directors in fulfilling their personal responsibilities for long-range achievements.

The Plan has been adopted and approved by the Board of Directors and shall become effective as of April 16, 2002, subject to the approval of the stockholders of the Company to the extent required, including with respect to those Participants to whom the 162(m) exemption of the Code would not otherwise apply.

**2. Definitions.**

As used in the Plan, the following definitions apply to the terms indicated below:

- (a) "Affiliate" means any entity if, at the time of granting of an Award (A) the Company, directly or indirectly, owns at least 50% of the combined voting power of all classes of stock of such entity or at least 50% of the ownership interests in such entity or (B) such entity, directly or indirectly, owns at least 50% of the combined voting power of all classes of stock of the Company.
- (b) "Agreement" shall mean either the written agreement between the Company and a Participant or a written notice from the Company to a Participant evidencing an Award.
- (c) "Award" shall mean any Option, Restricted Stock, Phantom Stock, Stock Bonus or Other Award granted pursuant to the terms of the Plan.
- (d) "Board of Directors" shall mean the Board of Directors of McLeodUSA Incorporated.
- (e) "Code" shall mean the Internal Revenue Code of 1986, as amended from time to time, and any regulations promulgated thereunder.
- (f) "Committee" shall mean, at the discretion of the Board of Directors, the full Board of Directors or a committee of the Board of Directors, which shall consist of two or more persons, each of whom, unless otherwise determined by the Board of Directors, is an "outside director" within the meaning of Section 162(m) of the Code and a "nonemployee director" within the meaning of Rule 16b-3.
- (g) "Company" shall mean McLeodUSA Incorporated, a Delaware corporation, and, where appropriate, each of its Affiliates.
- (h) "Company Stock" shall mean the common stock of the Company, par value \$0.01 per share.
- (i) "Covered Employee" shall have the meaning set forth in Section 162(m) of the Code.
- (j) "Effective Date" shall mean April 16, 2002.

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(k)

"Exchange Act" shall mean the Securities Exchange Act of 1934, as amended from time to time.

(l)

The "Fair Market Value" of a share of Company Stock shall mean the average of the high and low price of Company Stock as quoted on NASDAQ Automated Quotation System and published in The Wall Street Journal with respect to the date on which the fair market value is to be determined, or if there is no trading of Company Stock on such date, such price on the next date on which there is trading in such shares. In the event that shares of Company Stock are not quoted on such system or traded in a similar market, Fair Market Value shall be determined by the Board of Directors in good faith.

(m)

"Incentive Stock Option" shall mean an Option that is an "incentive stock option" within the meaning of Section 422 of the Code, or any successor provision, and that is designated b