BELLSOUTH CORP
Form 10-Q
May 05, 2005

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2005

OR

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

For the transition period from to

Commission file number 1-8607

BELLSOUTH CORPORATION
(Exact name of registrant as specified in its charter)

Georgia (State of Incorporation)	58-1533433 (I.R.S. Employer Identification Number)
1155 Peachtree Street, N. E., Atlanta, Georgia (Address of principal executive offices)	30309-3610 (Zip Code)

Registrant's telephone number 404-249-2000

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes __X__ No

At April 29, 2005, 1,831,018,173 common shares were outstanding.

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PART I - FINANCIAL INFORMATION

BELLSOUTH CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(IN MILLIONS, EXCEPT PER SHARE AMOUNTS)
(Unaudited)

	For the Three Months Ended March 31, 2004	2005
Operating Revenues:		
Communications Group..........................	$ 4,488	$ 4,593
Advertising & Publishing Group	479	488
All other	9	10
Total Operating Revenues	4,976	5,091
Operating Expenses:		

Cost of services and products (excludes depreciation and amortization shown separately below)	1,798	1,920
Selling, general, and administrative expenses	909	894
Depreciation and amortization	898	918
Provisions for restructuring	13	7
Total Operating Expenses	3,618	3,739
Operating income	1,358	1,352
Interest expense	215	291
Net earnings (losses) of equity affiliates	104	(80)
Gain on sale of operations	462	--
Other income (expense), net	64	56
Income from Continuing Operations Before Income Taxes and Discontinued Operations	1,773	1,037
Provision for Income Taxes	623	354
Income from Continuing Operations Before Discontinued Operations	1,150	683
Income (Loss) from Discontinued Operations, Net of Tax	449	381
Net Income	$ 1,599	$ 1,064
Weighted-Average Common Shares Outstanding:		
Basic	1,832	1,831
Diluted	1,838	1,836
Dividends Declared Per Common Share	$ 0.25	$ 0.27
Basic Earnings Per Share:		
Income from Continuing Operations Before Discontinued Operations	$ 0.63	$ 0.37
Discontinued Operations, net of tax	0.25	0.21
Net Income*	$ 0.87	$ 0.58
Diluted Earnings Per Share:		
Income from Continuing Operations Before Discontinued Operations	$ 0.63	$ 0.37
Discontinued Operations, net of tax	0.24	0.21
Net Income	$ 0.87	$ 0.58

*Net income per share may not sum due to rounding

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

BELLSOUTH CORPORATION
CONSOLIDATED BALANCE SHEETS
(IN MILLIONS, EXCEPT PER SHARE AMOUNTS)

	December 31, 2004	March 31, 2005 (unaudited)
ASSETS		
Current Assets :		
Cash and cash equivalents	$ 680	$ 516
Short-term investments	16	--
Accounts receivable, net of allowance for uncollectibles of $317 and $291	2,559	2,467
Material and supplies	321	308
Other current assets	1,055	907
Assets of discontinued operations	1,068	--
Total current assets	5,699	4,198
Investments in and advances to Cingular	22,771	22,265
Property, plant and equipment, net	22,039	21,913
Other assets	7,400	7,512
Intangible assets, net	1,587	1,557
Total assets	$ 59,496	$ 57,445
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Debt maturing within one year	$ 5,475	$ 4,149
Accounts payable	1,047	994
Other current liabilities	3,018	3,049
Liabilities of discontinued operations	830	--
Total current liabilities	10,370	8,192
Long-term debt	15,108	14,669
Noncurrent liabilities:		
Deferred income taxes	6,492	6,351
Other noncurrent liabilities	4,460	4,557
Total noncurrent liabilities	10,952	10,908
Shareholders' equity:		
Common stock, $1 par value (8,650 shares authorized; 1,831 and 1,831 shares outstanding)	2,020	2,020
Paid-in capital	7,840	7,810
Retained earnings	19,267	19,802
Accumulated other comprehensive income		

(loss)	(157)	(80)
Shares held in trust and treasury	(5,904)	(5,876)
Total shareholders' equity	23,066	23,676
Total liabilities and shareholders' equity	$ 59,496	$ 57,445

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

BELLSOUTH CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN MILLIONS)
(Unaudited)

	For the Three Months Ended March 31, 2004	2005
Cash Flows from Operating Activities:		
Income from continuing operations before discontinued operations	$ 1,150	$ 683
Adjustments to reconcile income to cash provided by operating activities from continuing operations:		
Depreciation and amortization	898	918
Provision for uncollectibles	115	85
Net losses (earnings) of equity affiliates	(104)	80
Deferred income taxes and investment tax credits	169	(45)
Pension income	(121)	(133)
Stock-based compensation expense	28	25
Gain on sale of operations	(462)	--
Net Change in:		
Accounts receivable and other current assets	(8)	(84)
Accounts payable and other current liabilities	56	23
Deferred charges and other assets	(25)	20
Other liabilities and deferred credits	9	103
Other reconciling items, net	23	43
Net cash provided by operating activities from continuing operations	1,728	1,718
Cash Flows from Investing Activities:		
Capital expenditures	(635)	(750)
Purchases of short-term investments	(824)	(12)
Proceeds from sale of short-term investments	558	28

Proceeds from sale of operations	525	919
Purchases of debt and equity securities	(140)	(32)
Proceeds from sale of debt and equity securities	34	10
Proceeds from repayment of loans and advances	109	402
Other investing activities, net	(22)	(5)
Net cash provided by (used for) investing activities from continuing operations	(395)	560
Cash Flows from Financing Activities:		
Net borrowings (repayments) of short-term debt	(362)	(1,093)
Repayments of long-term debt	(7)	(669)
Dividends paid	(457)	(494)
Purchase of treasury shares	--	(77)
Other financing activities, net	48	6
Net cash used in financing activities from continuing operations	(778)	(2,327)
Net increase (decrease) in cash and cash equivalents from continuing operations	555	(49)
Net increase (decrease) in cash and cash equivalents from discontinued operations	(9)	(115)
Net increase (decrease) in cash and cash equivalents	546	(164)
Cash and cash equivalents at beginning of period	2,947	680
Cash and cash equivalents at end of period	$ 3,493	$ 516

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

BELLSOUTH CORPORATION
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME
(IN MILLIONS)
(Unaudited)

	Number of Shares		Amou		
	Common Stock	(a) Shares Held in Trust and Treasury	Common Stock	Paid-in Capital	Retained Earnings

Balance at December 31, 2003	2,020	(190)	$ 2,020	$ 7,729	$ 16,540
Net Income					1,599
Other comprehensive income, net of tax					
Total comprehensive income					
Dividends declared					(457)
Share issuances for employee benefit plans		4		(60)	(56)
Stock-based compensation				30	
Tax benefit related to stock options				9	
Balance at March 31, 2004	2,020	(186)	$ 2,020	$ 7,708	$ 17,626
Balance at December 31, 2004	2,020	(189)	$ 2,020	$ 7,840	$ 19,267
Net Income					1,064
Other comprehensive income, net of tax					
Total comprehensive income					
Dividends declared					(494)
Purchase of treasury stock		(3)			
Share issuances for employee benefit plans		3		(55)	(35)
Stock-based compensation				25	
Balance at March 31, 2005	2,020	(189)	$ 2,020	$ 7,810	$ 19,802

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

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)
(Unaudited)

NOTE A - PREPARATION OF INTERIM FINANCIAL STATEMENTS

In this report, BellSouth Corporation and its subsidiaries are referred to as "we" or "BellSouth."

The accompanying unaudited consolidated financial statements have been prepared based upon Securities and Exchange Commission (SEC) rules that permit reduced disclosure for interim periods. In our opinion, these statements include all adjustments necessary for a fair presentation of the results of the interim periods presented. All adjustments are of a normal recurring nature unless otherwise disclosed. Revenues, expenses, assets and liabilities can vary during each quarter of the year. Therefore, the results and trends in these interim financial statements may not be the same as those for the full year. For a more complete discussion of our significant accounting policies and other information, you should read this report in conjunction with the consolidated financial statements included in our latest annual report on Form 10-K.

Certain amounts within the prior year's information have been reclassified to conform to the current year's presentation.

NOTE B - RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In December 2004, the FASB issued SFAS No. 123 (Revised 2004), "Share-Based Payment." This standard amends and clarifies the accounting for stock compensation plans under SFAS 123, "Accounting for Stock-Based Compensation," which we adopted effective January 1, 2003. During the first quarter, the FASB revised the adoption date of this revised statement effective the first annual reporting period that begins after June 15, 2005. Accordingly, we will adopt this revised statement on January 1, 2006. We do not expect the adoption of this statement to have a material impact on our results of operations, financial position or cash flows.

In March 2005, the FASB issued FASB Interpretation No. 47, "Accounting for Conditional Asset Retirement Obligations" (FIN 47). FIN 47 clarifies that the term conditional asset retirement obligation as used in FASB Statement No. 143, "Accounting for Asset Retirement Obligations," refers to a legal obligation to perform an asset retirement activity in which the timing and (or) method of settlement are conditional on a future event that may or may not be within the control of the entity. The obligation to perform the asset retirement activity is unconditional even though uncertainty exists about the timing and (or) method of settlement. Uncertainty about the timing and (or) method of settlement of a conditional asset retirement obligation should be factored into the measurement of the liability when sufficient information exists. FIN 47 also clarifies when an entity would have sufficient information to reasonably estimate the fair value of an asset retirement obligation. FIN 47 is effective no later than the end of fiscal years ending after December 15, 2005. We are currently evaluating the impact the standard will have on BellSouth's financial position, results of operations and cash flows.

NOTE C - EARNINGS PER SHARE

Basic earnings per share are computed based on the weighted-average number of common shares outstanding during each year. Diluted earnings per share are based on the weighted-average number of common shares outstanding plus net incremental shares arising out of employee stock options and benefit plans. The earnings amounts used for per-share calculations are the same for both the basic and diluted methods. The following is a reconciliation of the weighted-average share amounts (in millions) used in calculating earnings per share:

	For the Three Months Ended March 31,	
	2004	2005
Basic common shares outstanding	1,832	1,831
Incremental shares from stock options and benefit plans............................	6	5
Diluted common shares outstanding	1,838	1,836
	=====	=====
Stock options excluded from the computation ..	80	78

Options with an exercise price greater than the average market price of the common stock for the periods presented or that have an anti-dilutive effect on the computation are excluded from the calculation of diluted earnings per share.

NOTE D - DISCONTINUED OPERATIONS

In March 2004, we signed an agreement with Telefonica Moviles, S.A., the wireless affiliate of Telefonica, S.A. (Telefonica), to sell all of our interests in Latin America. During January 2005, we closed on the sale of the operations in the remaining two Latin American countries (Argentina and Chile) for proceeds of $1,079 and a gain of $390, net of tax. The gain includes the recognition of cumulative foreign currency translation losses of $68.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)
(Unaudited)

NOTE D - DISCONTINUED OPERATIONS (Continued)

Summarized results of operations for the discontinued operations are as follows:

	For the Three Months Ended March 31, 2004	2005
Revenue	$ 677	$ 66
Operating income (loss)	$ 71	$ (5)
Gain on sale of operations	$ --	$ 629
Income tax (benefit) expense	$(405)	$ 235
Income from discontinued operations	$ 449	$ 381

Note E - INVESTMENTS AND ADVANCES TO CINGULAR

Investment

We own an approximate 40% economic interest in Cingular, a joint venture with SBC Communications. Because we exercise influence over the financial and operating policies of Cingular, we use the equity method of accounting for this investment. Under the equity method of accounting, we record our proportionate share of Cingular's earnings in our consolidated statements of income. These earnings are included in the caption "Net earnings (losses) of equity affiliates."

The following table displays the summary financial information of Cingular. These amounts are shown on a 100% basis.

	December 31, 2004	March 31, 2005
Balance Sheet Information:		
Current assets	$ 5,570	$ 4,906
Noncurrent assets	$ 76,668	$75,566
Current liabilities	$ 7,983	$ 7,579
Noncurrent liabilities	$ 29,110	$27,980
Minority interest	$ 609	$ 619
Members' capital	$ 44,536	$ 44,294

	For the Three Months Ended March 31, 2004	2005
	----	----

Income Statement Information:		
Revenues	$3,967	$8,229
Operating income	$ 550	$ 114
Net income (loss)	$ 215	$ (240)

As of March 31, 2005, our book investment exceeded our proportionate share of the net assets of Cingular by $503.

Advance

We have an advance to Cingular that, with interest, totaled $3,792 at December 31, 2004 and $3,773 at March 31, 2005. This advance earns an interest rate of 6.0% per annum and matures on June 30, 2008.

Revolving Line of Credit

BellSouth and SBC provide unsubordinated short-term financing on a pro rata basis for Cingular's ordinary course of business cash requirements based upon Cingular's budget and forecasted cash needs. Borrowings bear interest at 1-Month LIBOR plus 0.05% payable monthly. Borrowings from BellSouth under the revolving credit line, including interest, were $668 at December 31, 2004 and $271 at March 31, 2005.

Provision of Services

We also generate revenues from Cingular in the ordinary course of business for the provision of local interconnection services, long distance services, sales agency fees and customer billing and collection fees.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)
(Unaudited)

Note E - INVESTMENTS AND ADVANCES TO CINGULAR (Continued)

Interest and Revenue Earned from Cingular

	For the Three Months Ended March 31,	
	2004	2005
Revenues	$ 117	$ 174
Interest income on advances	$ 57	$59

Interest income on advances is offset by a like amount of interest expense recorded by Cingular and reported in our financial statements in the caption "Net earnings (losses) of equity affiliates."

Receivables and payables incurred in the ordinary course of business are recorded on our balance sheets as follows:

	December 31, 2004	March 31, 2005
Receivable from Cingular	$ 56	$66
Payable to Cingular	$ 44	$46

NOTE F - OTHER ASSETS

Investment in and Advance to Sonofon

On February 12, 2004, we closed on a previously announced agreement to sell our interest in Danish wireless provider, Sonofon, for 3.68 billion Danish Kroner to Telenor ASA. We received 3.05 billion Danish Kroner, or $525, for our 46.5% equity stake and 630 million Danish Kroner, or $109, for our shareholder loan and accrued interest, reduced by a settlement of $17 associated with foreign currency swap contracts. As a result of these transactions, we recorded a gain of $462, or $295 net of tax, which included the recognition of cumulative foreign currency translation gains of $13.

NOTE G - DEBT

Early Redemption

On January 18, 2005, we redeemed $400 of 40-year, 6.75% semi-annual interest bonds, due October 15, 2033. The redemption price was 103.33% of the principal amount, and resulted in recognition of a loss of $22, or $14 net of tax, which includes $9 associated with fully expensing remaining discount and deferred debt issuance costs.

Subsequent Event

On April 18, 2005, we called $300 of 40-year, 7.625% semi-annual interest bonds, due May 15, 2035. The redemption price is 103.66% of the principal amount, and will result in the recognition of a loss in the second quarter of 2005 of $20, or $12 net of tax, which includes $9 associated with fully expensing remaining discount and deferred debt issuance costs.

NOTE H - WORKFORCE REDUCTION AND RESTRUCTURING

Based on ongoing challenges in the telecom industry, we periodically initiate workforce reductions and record charges for early termination benefits. We announced the termination of approximately 200 positions during the first quarter of 2005. Charges to earnings have been recognized in accordance with provisions of SFAS No. 112, "Employer's Accounting for Postemployment Benefits" (SFAS No. 112), and consisted primarily of cash severance and payroll taxes under pre-existing separation pay plans.

The following table summarizes activity associated with the workforce reduction and restructuring liability for the three months ended March 31, 2005:

Balance at December 31, 2004......	$ 25
Accruals.........................	9
Cash Payments	(12)
Adjustments......................	(2)
Balance at March 31, 2005.........	$20

Adjustments to the accrual are due to estimated demographics being different than actual demographics of employees that separated from the Company.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)
(Unaudited)

NOTE I - EMPLOYEE BENEFITS PLANS

Substantially all of our employees are covered by noncontributory defined benefit pension plans, as well as postretirement health and life insurance welfare plans ("other benefits").

The following details pension and postretirement benefit costs included in operating expenses (in cost of sales and selling, general and administrative expenses) in the accompanying Consolidated Statements of Income. Approximately 10% of these costs are capitalized to property, plant and equipment with labor related to network construction. We account for these costs in accordance with SFAS No. 87, "Employers' Accounting for Pensions" and SFAS No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions." Components of net periodic benefit costs for the three months ended March 31 were as follows:

	Pension Benefits		Other Benefits	
	2004	2005	2004	2005
Service cost	$ 44	$ 52	$ 12	$ 31
Interest cost	174	147	108	146
Expected return on plan assets	(329)	(322)	(80)	(84)
Amortizations:				
Unrecognized net obligation	--	--	25	18
Unrecognized prior service cost...	(11)	(10)	53	56
Unrecognized (gain) loss..........	1	--	20	26
Net periodic benefit cost (income)..	(121)	(133)	138	193

Employer Contributions

During the three months ended March 31, 2005, we made no contributions to our pension plans and anticipate no funding for the remainder of 2005. During the three months ended March 31, 2005, we have contributed $116 to fund other benefits (primarily retiree medical) and expect to contribute approximately $335 to $385 of funding for other benefits during the remainder of 2005.

Cash Balance Pension Plan

In July 2003, a Federal district court in Illinois ruled that the benefit formula used in International Business Machines Corporation's (IBM) cash balance pension plan violated the age discrimination provisions of ERISA. The IBM decision conflicts with decisions of at least two other district courts, including most recently a June 2004 decision of the Federal district court in Maryland in a case involving ARINC, Inc. Proposed regulations validating the cash balance design have been withdrawn by the Treasury Department while Congress considers legislative action to clarify the legal status of cash balance plans under age discrimination rules. At this time, it is unclear what effect, if any, these decisions or Congressional action may have on our tax-qualified cash balance pension plans or our financial condition.

NOTE J - SEGMENT INFORMATION

We have three reportable operating segments: (1) Communications Group; (2) Domestic Wireless; and (3) Advertising and Publishing. We own an approximate 40% economic interest in Cingular Wireless, and share joint control of the venture with SBC. We account for the investment under the equity method. For management purposes we evaluate our domestic wireless segment based on our proportionate share of Cingular's results. Accordingly, results for our domestic wireless segment reflect the proportional consolidation of 40% of Cingular's results.

Beginning in the first quarter of 2005, BellSouth began to include various corporate entities, the largest of which is the Information Technology Group, in the Communications Group segment for financial reporting purposes. These entities previously billed their costs to the Communications Group. This change simplifies management reporting, is principally timing in nature and does not affect the consolidated financial statements. Prior period segment operating results were recast to reflect the reporting change.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)
(Unaudited)

NOTE J - SEGMENT INFORMATION (Continued)

The following table provides information for each operating segment:

	For the Three Months Ended March 31, 2004	2005
Communications Group		
External revenues....................	$ 4,538	$ 4,593
Intersegment revenues	26	25
Total segment revenues...........	$ 4,564	$ 4,618
Segment operating income	$ 1,187	$ 1,117
Segment net income	$ 697	$ 664
Domestic Wireless		
External revenues	$ 1,587	$ 3,292
Intersegment revenues..........................	--	--
Total segment revenues...........	$ 1,587	$ 3,292
Segment operating income	$ 224	$ 88
Segment net income (loss)........................	$ 59	$ (33)
Advertising and Publishing Group		
External revenues	$ 479	$ 488
Intersegment revenues	3	3
Total segment revenues...........	$ 482	$ 491
Segment operating income	$ 239	$ 231
Segment net income	$ 147	$ 141

RECONCILIATION TO CONSOLIDATED FINANCIAL INFORMATION

	For the Three Months Ended March 31, 2004	2005
Operating revenues		
Total reportable segments	$ 6,633	$ 8,401
Cingular proportional consolidation.....................	(1,587)	(3,292)
South Carolina settlement	(50)	--
Corporate, eliminations and other ...	(20)	(18)

Total consolidated	$ 4,976	$ 5,091
Operating income		
Total reportable segments	$ 1,650	$ 1,436
Cingular proportional consolidation	(224)	(88)
South Carolina settlement	(53)	--
Restructuring charge	(13)	--
Corporate, eliminations and other	(2)	4
Total consolidated	$ 1,358	$ 1,352
Net Income		
Total reportable segments	$ 903	$ 772
Net gain on sale of operations	295	--
South Carolina settlement	(33)	--
Restructuring charge	(8)	--
Wireless merger integration costs	--	(21)
Early extinguishment of debt	--	(14)
Discontinued operations	449	381
Corporate, eliminations and other	(7)	(54)
Total consolidated	$ 1,599	$ 1,064

The Cingular proportional consolidation shown above represents the amount necessary to reconcile the proportional results of Cingular to GAAP results. Reconciling items are transactions or events that are included in reported consolidated results but are excluded from segment results due to their nonrecurring or nonoperational nature.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)
(Unaudited)

Note K - other comprehensive income

Accumulated other comprehensive income (loss) is comprised of the following components:

	December 31, 2004	March 31, 2005
Cumulative foreign currency translation adjustments	$ (79)	$ 2
Minimum pension liability adjustment	(129)	(129)
Net unrealized losses on derivatives	(12)	(5)
Net unrealized gains (losses) on securities	63	52
	$(157)	$ (80)

Accumulated other comprehensive income (loss) for our discontinued operations included in the amounts above was $(77) as of December 31, 2004 and zero as of March 31, 2005.

Total comprehensive income details are presented in the table below.

	For the Three Months Ended March 31, 2004	2005
Net Income	$ 1,599	$ 1,064
Foreign currency translation:		
Adjustments, net of tax of $182 and $0	113	13
Sale of foreign entities, net of tax of $0 and $42	(13)	68
	100	81
Deferred gains (losses) on derivatives:		
Deferred gains (losses), net of tax of $1 and $4	1	7
Reclassification adjustment for (gains) losses included in net income, net of tax of $0	3	--
	4	7
Unrealized gains (losses) on securities:		
Unrealized holdings gains (losses), net of tax of $5 and $(5)	8	(10)
Reclassification adjustment for (gains) losses included in net income, net of tax of $1 and $(1)	2	(1)
	10	(11)
Total comprehensive income	$ 1,713	$ 1,141

NOTE L - CONTINGENCIES

GUARANTEES

In most of our sale and divestiture transactions, we indemnify the purchaser for various items including labor and general litigation as well as certain tax matters. Generally, the terms last one to five years for general and specific indemnities and for the statutory review periods for tax matters. The events or circumstances that would require us to perform under the indemnity are transaction and circumstance specific. We regularly evaluate the probability of having to incur costs associated with these indemnifications and have accrued for expected losses that are probable. In addition, in the normal course of business, we indemnify counterparties in certain agreements. The nature and terms of these indemnities vary by transaction. Historically, we have not incurred significant costs related to performance under these types of indemnities.

REGULATORY MATTERS

AT&T Prepaid Card

In February 2005, the FCC released an order finding that certain prepaid card services of AT&T were telecommunications services. The FCC held that revenue from the services would accordingly be subject to the same universal service fund and switched access charges as were all other similarly situated telecommunications services. AT&T has estimated in a securities filing that it had "saved" approximately $160 in universal service fund contributions and $340 in access charges through use of the prepaid card services that were the subject of the FCC decision. We believe that some of the improperly avoided access charges should have been paid to us for the use of our network. AT&T has not provided information sufficient for us to reasonably estimate access charge payments we may be owed. In addition, AT&T has

NOTE L - CONTINGENCIES (Continued)

appealed the FCC decision. Accordingly, no revenue has been recognized with respect to this matter in our consolidated financial statements.

Section 272 Claim

In December 2004, the FCC partially granted and otherwise dismissed claims brought by AT&T in July 2004 that two optional discount special access tariffs violated various provisions of the Communications Act. The FCC held that one of the tariffs, the Transport Savings Plan, was unlawful under Section 272 of the Act, which governs dealings between BST and our long distance affiliate. That tariff, originally filed in 1999, provided an overlay discount for carriers that accepted its terms, which included a five year commitment, a commitment for a defined amount of spending on special access, and shortfall charges if commitments were not met. The FCC held that the discount structure in the tariff was insufficiently related to cost, and unduly favored a class of carriers (including our long distance affiliate) with relatively lower volume special access spending, and discriminated against carriers with relatively higher volumes. The FCC dismissed the other claims associated with the Transport Savings Plan, and dismissed all claims associated with the second tariff. We did not agree with the FCC's finding, and appealed its decision to the D.C. Circuit Court of Appeals. AT&T appealed the portions of the decision unfavorable to it.

In March 2005, as part of a broader commercial agreement, we resolved the July 2004 claims of AT&T. Also in March 2005, we filed a new tariff which provided for customers to earn discounts similar to those under the Transport Savings Plan. Each party continues to maintain its appeal of the FCC decision, the outcomes of which are not expected to be material to our results of operations or cash flows.

LEGAL PROCEEDINGS

Employment Claim

On April 29, 2002, five African-American employees filed a putative class action lawsuit, captioned Gladys Jenkins et al. v. BellSouth Corporation, against the Company in the United States District Court for the Northern District of Alabama. The complaint alleges that BellSouth discriminated against current and former African-American employees with respect to compensation and promotions in violation of Title VII of the Civil Rights Act of 1964 and 42 USC. Section 1981. Plaintiffs purport to bring the claims on behalf of two classes: a class of all African-American hourly workers employed by BellSouth Telecommunications at any time since April 29, 1998, and a class of all African- American salaried workers employed by BellSouth Telecommunications at any time since April 29, 1998 in management positions at or below Job Grade 59/Level C. The plaintiffs are seeking unspecified amounts of back pay, benefits, punitive damages and attorneys' fees and costs, as well as injunctive relief. At this time, the likely outcome of the case cannot be predicted, nor can a reasonable estimate of the amount of loss, if any, be made.

Securities and ERISA Claims

From August through October 2002, several individual shareholders filed substantially identical class action lawsuits against BellSouth and three of its senior officers alleging violations of the federal securities laws. The cases have been consolidated in the United States District Court for the Northern District of Georgia and are captioned In re BellSouth Securities Litigation. Pursuant to the provisions of the Private Securities Litigation Reform Act of 1995, the court has appointed a Lead Plaintiff. The Lead Plaintiff filed a Consolidated and Amended Class Action Complaint in July 2003 on behalf of two putative classes: (1) purchasers of BellSouth stock during the period November 7, 2000 through February 19, 2003 (the class period) for alleged violations of Sections 10(b) and 20 of the Securities Exchange Act of 1934 and (2) participants in BellSouth's Direct Investment Plan during the class period for alleged violations of Sections 11, 12 and 15 of the Securities Act of 1933. Four outside directors were named as additional defendants. The Consolidated and Amended Class Action Complaint alleged that during the class period the Company (1) overstated the unbilled receivables balance of its Advertising & Publishing subsidiary; (2) failed to properly implement SAB 101 with regard to its recognition of Advertising & Publishing revenues; (3) improperly billed competitive local exchange carriers (CLEC) to inflate revenues; (4) failed to take a reserve for refunds that ultimately came due following litigation over late payment charges; and (5) failed to properly write down goodwill of its Latin American operations. On February 8, 2005, the district court dismissed the Exchange Act claims, except for those relating to the writedown of Latin American goodwill. On that date, the district court also dismissed the Securities Act claims, except for those relating to the writedown of Latin American goodwill, the allegations relating to unbilled receivables of the Company's Advertising & Publishing subsidiary, the implementation of SAB 101 regarding recognition of Advertising & Publishing revenues and alleged improper billing of CLECs. The plaintiffs are seeking an unspecified amount of damages, as well as attorneys' fees and costs. At this time, the likely outcome of the case cannot be predicted, nor can a reasonable estimate of loss, if any, be made.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)
(Unaudited)

NOTE L - CONTINGENCIES (Continued)

In February 2003, a similar complaint was filed in the Superior Court of Fulton County, Georgia on behalf of participants in BellSouth's Direct Investment Plan alleging violations of Section 11 of the Securities Act. Defendants removed this action to federal court pursuant to the provisions of the Securities Litigation Uniform Standards Act of 1998. In July 2003, the federal court issued a ruling that the case should be remanded to Fulton County Superior Court. The Fulton County Superior Court has stayed the case pending resolution of the federal case. The plaintiffs are seeking an unspecified amount of damages, as well as attorneys' fees and costs. At this time, the likely outcome of the case cannot be predicted, nor can a reasonable estimate of loss, if any, be made.

In September and October 2002, three substantially identical class action lawsuits were filed in the United States District Court for the Northern District of Georgia against BellSouth, its directors, three of its senior officers, and other individuals, alleging violations of the Employee Retirement Income Security Act (ERISA). The cases have been consolidated and on April 21, 2003, a Consolidated Complaint was filed. The plaintiffs, who seek to represent a putative class of participants and beneficiaries of BellSouth's 401(k) plans (the Plans), allege in the Consolidated Complaint that the company and the individual defendants breached their fiduciary duties in violation of ERISA, by among other things, (1) failing to provide accurate information to the Plans' participants and beneficiaries; (2) failing to ensure that the Plans' assets were invested properly; (3) failing to monitor the Plans' fiduciaries; (4) failing to disregard Plan directives that the defendants knew or should have known were imprudent and (5) failing to avoid conflicts of interest by hiring independent fiduciaries to make investment decisions. The plaintiffs are seeking an unspecified amount of damages, injunctive relief, attorneys' fees and costs. Certain underlying factual allegations regarding BellSouth's Advertising & Publishing subsidiary and its former Latin American operation are substantially similar to the allegations in the putative securities class action captioned In re BellSouth Securities Litigation, which is described above. At this time, the likely outcome of the cases cannot be predicted, nor can a reasonable estimate of loss, if any, be made.

Antitrust Claims

In December 2002, a consumer class action alleging antitrust violations of Section 1 of the Sherman Antitrust Act was filed against BellSouth, Verizon, SBC and Qwest, captioned William Twombley, et al v. Bell Atlantic Corp., et al, in Federal Court in the Southern District of New York. The complaint alleged that defendants conspired to restrain competition by "agreeing not to compete with one another and otherwise allocating customers and markets to one another." The plaintiffs are seeking an unspecified amount of treble damages and injunctive relief, as well as attorneys' fees and expenses. In October 2003, the district court dismissed the complaint for failure to state a claim and the case is now on appeal.

In June 2004, the U.S. Court of Appeals for the 11th Circuit affirmed the District Court's dismissal of most of the antitrust and state law claims brought by a plaintiff CLEC in a case captioned Covad Communications Company, et al v. BellSouth Corporation, et al. The appellate court, however, permitted a price squeeze claim and certain state tort claims to proceed. At this time, the likely outcome of the case cannot be predicted, nor can a reasonable estimate of loss, if any, be made.

OTHER CLAIMS

We are subject to claims arising in the ordinary course of business involving allegations of personal injury, breach of contract, anti-competitive conduct, employment law issues, regulatory matters and other actions. BST is also subject to claims attributable to pre-divestiture events, including environmental liabilities, rates and contracts. Certain contingent liabilities for pre-divestiture events are shared with AT&T Corp. While complete assurance cannot be given as to the outcome of these claims, we believe that any financial impact would not be material to our results of operations, financial position or cash flows.

NOTE M - SUBSIDIARY FINANCIAL INFORMATION

We have fully and unconditionally guaranteed all of the outstanding debt securities of BellSouth Telecommunications, Inc. (BST), which is a 100% owned subsidiary of BellSouth. In accordance with SEC rules, we are providing the following condensed consolidating financial information. BST is listed separately because it has debt securities, registered with the SEC, that we have guaranteed. The Other column represents all other wholly owned subsidiaries excluding BST and BST subsidiaries. The Adjustments column includes the necessary amounts to eliminate the intercompany balances and transactions between BST, Other and Parent and to consolidate wholly owned subsidiaries to reconcile to our consolidated financial information.

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)
(Unaudited)

NOTE M - SUBSIDIARY FINANCIAL INFORMATION (Continued)

Condensed Consolidating Statements of Income

	For the Three Months Ended March 31, 2004				
	BST	Other	Parent	Adjustments	Total
Total operating revenues	$4,188	$1,517	$ --	$ (729)	$4,976
Total operating expenses	3,643	1,074	(6)	(1,093)	3,618
Operating income	545	443	6	364	1,358
Interest expense	124	6	139	(54)	215
Equity in earnings	256	103	1,196	(1,451)	104
Other income (expense), net	(1)	522	23	(18)	526
Income before income taxes and discontinued operations	676	1,062	1,086	(1,051)	1,773
Provision (benefit) for income taxes	152	387	(64)	148	623
Income from continuing operations	524	675	1,150	(1,199)	1,150
Discontinued operations, net of tax	--	449	449	(449)	449
Net income (loss)	$ 524	$1,124	$ 1,599	$(1,648)	$ 1,599

	For the Three Months Ended March 31, 2005				
	BST	Other	Parent	Adjustments	Total
Total operating revenues	$ 4,190	$1,711	$ --	$ (810)	$ 5,091
Total operating expenses	3,700	1,247	14	(1,222)	3,739
Operating income	490	464	(14)	412	1,352
Interest expense	118	--	225	(52)	291
Equity in earnings	276	(78)	791	(1,069)	(80)
Other income (expense), net	(18)	48	57	(31)	56
Income before income taxes and discontinued operations	630	434	609	(636)	1,037
Provision (benefit) for income taxes	121	148	(74)	159	354

Income from continuing operations............	509	286	683	(795)	683
Discontinued operations, net of tax..............	--	381	381	(381)	381
Net income (loss)	$ 509	$ 667	$ 1,064	$(1,176)	$ 1,064

Condensed Consolidating Balance Sheets

December 31, 2004

	BST	Other	Parent	Adjust- ments	Total	BST	Ot
ASSETS							
Current assets:							
Cash and cash equivalents	$ 7	$ 405	$ 265	$ 3	$ 680	$ 5	$
Short-term investments	--	--	16	--	16	--	
Accounts receivable, net	75	1,005	2,918	(1,439)	2,559	65	1
Other current assets	528	4,418	144	(3,714)	1,376	415	
Assets of discontinued operations	--	1,068	--	--	1,068	--	
Total current assets	610	6,896	3,343	(5,150)	5,699	485	1
Investments in and advances to Cingular	--	21,232	1,539	--	22,771	--	21
Property, plant and equipment, net	21,339	665	3	32	22,039	21,245	
Deferred charges and other assets	8,782	747	39,305	(41,434)	7,400	8,808	
Intangible assets, net	1,072	391	9	115	1,587	1,047	
Total assets ....$	31,803	$ 29,931	$ 44,199	$(46,437)	$ 59,496	$31,585	$24
LIABILITIES AND SHAREHOLDERS' EQUITY							
Current liabilities:							
Debt maturing within one year .$	3,016	$ 15	$ 4,248	$(1,804)	$ 5,475	$ 3,993	$
Other current liabilities	3,941	1,165	4,905	(5,946)	4,065	3,070	1
Liabilities of discontinued operations..................	--	830	--	--	830	--	
Total current liabilities	6,957	2,010	9,153	(7,750)	10,370	7,063	1

Long-term debt	3,704	107	11,874	(577)	15,108	3,280	
Noncurrent liabilities:							
Deferred income taxes	5,063	1,735	(490)	184	6,492	4,983	1
Other noncurrent liabilities ..	2,974	791	596	99	4,460	3,037	
Total noncurrent liabilities ..	8,037	2,526	106	283	10,952	8,020	2
Shareholders' equity...........	13,105	25,288	23,066	(38,393)	23,066	13,222	20
Total liabilities and shareholders' equity	$31,803	$29,931	$44,199	$(46,437)	$59,496	$31,585	$24

BELLSOUTH CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS AND AS OTHERWISE INDICATED)
(Unaudited)

NOTE M - SUBSIDIARY FINANCIAL INFORMATION (Continued)

Condensed Consolidating Cash Flow Statements

	For the Three Months Ended Mar		
	BST	Other	Parent
Cash flows from continuing operations:			
Cash flows from operating activities	$ 1,233	$ 280	$ 988
Cash flows from investing activities	(653)	583	372
Cash flows from financing activities	(552)	(845)	(760)
Cash flows from discontinued operations	--	(9)	--
Net (decrease) increase in cash	$ 18	$ 9	$ 600

	For the Three Months Ended Mar		
	BST	Other	Parent

Cash flows from continuing operations:			
Cash flows from operating activities	$ 1,563	$ 373	$ 451
Cash flows from investing activities	(716)	(207)	1,210
Cash flows from financing activities	(849)	(257)	(1,651)
Cash flows from discontinued operations	--	(115)	--
Net (decrease) increase in cash	$ (2)	$ (206)	$ 10

BELLSOUTH CORPORATION
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS
(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

For a more complete understanding of our industry, the drivers of our business and our current period results, you should read the following Management's Discussion and Analysis of Financial Condition and Results of Operations in conjunction with our annual report on Form 10-K for the year ended December 31, 2004 and our other filings with the SEC.

Overview

We are a Fortune 100 company with annual revenues of over $20 billion. Our core business is wireline communications and our largest customer segment is the retail consumer. We have interests in wireless communications through our ownership of approximately 40% of Cingular Wireless (Cingular), the nation's largest wireless company based on number of customers. We also operate one of the largest directory advertising businesses in the United States. The great majority of our revenues are generated based on monthly recurring services.

We operate much of our business in one of the country's strongest regional economies, where the population is increasing, real income growth is outpacing the national average and a diverse mix of businesses require advanced information and communication technology solutions. The Southeast is a positive net migration region, with net migration averaging almost 500 thousand annually. The region's real income is expected to grow 10% to 15% faster than the national average in the next five years.

INDUSTRY DYNAMICS

The communications industry has experienced a very difficult period of contraction brought on by over-investment in the late 1990s that created significant excess capacity with many companies competing for the same business. Demand in the traditional voice business has been negatively impacted by the proliferation of wireless services led by one-rate pricing plans that include a large bucket of minutes and free roaming and long-distance, the popularity of e-mail and instant messaging, technological advances such as cable and DSL, that obviate the need for additional telephone lines. After a period of significant growth in the 1990s, access lines, a key driver of our business, have declined steadily since 2001.

Based on comparisons to penetration rates in other parts of the world, there is still significant growth potential in the wireless market in the United States. There are currently five national wireless companies engaging in aggressive competition in a growing market. The intense competition has driven down pricing, increased costs due to customer churn and increased wireless usage as companies attempt to differentiate their service plans. Meanwhile, significant capital is being invested in networks to meet increasing demand and to upgrade capabilities in anticipation of the development of new data applications.

REGULATION AND COMPETITION

Our wireless and wireline businesses are subject to vigorous competition. In addition, both are subject to regulation.

Because of changes to federal law in the early 1990s, our wireless business is now subject to somewhat more rational regulation than our wireline business. The legal changes generally preempted states from exercising any entry or rate regulation on commercial mobile services, while allowing states to regulate other terms and conditions. Our wireline business is subject to dual state and federal regulation. The Telecommunication Act of 1996 produced additional regulation of our wireline business. Since its passage, the FCC has pursued a course of sharing (unbundling) our network with competitors, and has prescribed a pricing policy (TELRIC) that does not permit fair cost recovery. The unbundling rules have been invalidated by the courts on three separate occasions, but not before the unbundling required by its invalid policies had been generally implemented in our contracts with competitors.

In February 2005, the FCC released its Triennial Review Remand Order (TRRO), which effectively eliminated UNE-P on a nation-wide basis (following a 1-year transition period) and provided limited unbundling relief on high-capacity loops and transport where certain competitive thresholds had been met. The TRRO became effective on March 11, 2005. In response to this decision as well as previous findings of the FCC and the courts, BellSouth has entered into commercial agreements with over 100 competitors for services that replace UNE-P at negotiated rates. In addition, the FCC is reviewing other regulations that impact our business, including: the TELRIC methodology that underpins UNE pricing rules for remaining UNEs; intercarrier compensation and access charge reform; and regulation of voice over Internet Protocol (VoIP).

We also obtained some broadband freedom through a recent FCC decision not to require unbundling of installations that bring fiber optic technology within 500 feet of a customer's premises. We equipped more than 100,000 homes with this technology in 2004, and expect to continue deployments in 2005.

Despite these successes, our wireline business remains more regulated than competing businesses that use cable or wireless technologies. We will accordingly continue to encourage regulatory reform in every appropriate forum.

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

ACQUISITIONS AND DISPOSITIONS

On October 26, 2004, Cingular completed its previously announced acquisition of AT&T Wireless. Since the close, Cingular has had excellent success in the marketplace, gaining over 2.8 million new customers. Its new advertising campaigns combined with improvements in customer service and network coverage are driving customer loyalty and growth. Customer churn has reduced appreciably, integration efforts are well underway and we expect cost synergies to begin to contribute to margin expansion later in 2005. This acquisition substantially increases BellSouth's participation in the domestic wireless industry, bringing wireless to 40 percent of our proportional revenues including Cingular.

On March 5, 2004, we signed an agreement with Telefonica Moviles, S.A., the wireless affiliate of Telefonica, S.A., to sell all of our interests in our Latin American operations. During October 2004, we closed on the sale of 8 of the 10 properties: Venezuela, Colombia, Ecuador, Peru, Guatemala, Nicaragua, Uruguay and Panama. During January 2005, we closed on the sale of the remaining properties in Argentina and Chile.

HIGHLIGHTS AND OUTLOOK

Consolidated revenue growth is being driven by long distance and DSL services. We added approximately 455,000 long distance customers in the first quarter of 2005 to total almost 6.5 million at March 31, 2005, while net new DSL subscriber additions of 253,000 brought our total to over 2.3 million at March 31, 2005. Access lines continued to decline during the first quarter of 2005 with retail access lines down 61,000, which included positive business line growth of 6,000. UNE-P access lines resold by BellSouth competitors were down 95,000 compared to year-end 2004.

Our cost structure is heavily weighted towards labor and fixed asset related costs. In order to sustain margins, we have to adjust our workforce as market share of access lines shifts. Since the beginning of 2001, we have reduced our domestic workforce by almost 18,000 employees, or 22%. Maintaining current operating margin levels going forward will be challenging as competition intensifies and we are forced to achieve continued increases in productivity. This challenge was evident during the first quarter of 2005 as margins were down 70 basis points from the first quarter of 2004. While there have been some encouraging developments on the regulatory front, there will be other events such as increasing healthcare costs, continued loss of lines to wireless substitution and the roll-out of Voice over Internet Protocol (VoIP) telephony by cable providers that are likely to continue to put pressure on margins.

Cingular Wireless added more than 1.4 million customers in the first quarter of 2005, bringing its nationwide customer base to 50.4 million customers. Customer churn improved to 2.2 percent in the first quarter of 2005. Revenue growth on a pro forma basis exceeded 5 percent in the first quarter driven by subscriber growth partially offset by a decline in pro forma average revenue per user. Operating margins improved in the quarter as compared to the fourth quarter of 2004 due primarily to lower gross customer additions, increased revenues, and lower customer service expense. First quarter operating margins were negatively impacted sequentially due to the inclusion of expenses that were previously reported in equity earnings prior to the termination of Cingular's joint venture with T-Mobile.

Operating cash flow from continuing operations of $1,718 in the first quarter of 2005 was comparable to $1,728 in the first quarter of 2004. Capital expenditures were $750 in the first quarter of 2005 and $635 in the first quarter of 2004. The increase was driven by timing and investment in broadband infrastructure. In the next two years, operating cash flow will be negatively impacted by higher cash taxes as we see a reversal of the benefit derived in recent years associated with legislated tax incentives that provided for accelerated depreciation deductions that expired at the end of 2004.

Consolidated Results of Operations

Key financial and operating data for the three months ended March 31, 2004 and 2005 are set forth below. All references to earnings per share are on a diluted basis. The discussion of consolidated results should be read in conjunction with the discussion of results by segment directly following this section.

Following generally accepted accounting principles (GAAP), our financial statements reflect results for the Latin American operations as Discontinued Operations. The operational results and the gain associated with the sale of the Latin American businesses are presented on one line item in the income statement.

	For the Three Months Ended March 31, 2004	2005	Percent Change
Results of operations:			
Operating revenues	$ 4,976	$5,091	2.3%
Operating expenses			
Cost of services and products	1,798	1,920	6.8%
Selling, general, and administrative expenses	909	894	-1.7%
Depreciation and amortization	898	918	2.2%
Provision for restructuring and asset impairments	13	7	-46.2%
Total operating expenses	3,618	3,739	3.3%
Operating income	1,358	1,352	-0.4%
Interest expense	215	291	35.3%
Net (losses) earnings of equity affiliates	104	(80)	-176.9%
Gain (loss) on sale of operations	462	--	*
Other income (expense), net	64	56	-12.5%
Income from continuing operations before income taxes and discontinued operations	1,773	1,037	-41.5%
Provision for income taxes	623	354	-43.2%
Income from continuing operations before discontinued operations	1,150	683	-40.6%
Income (loss) from discontinued operations, net of tax	449	381	-15.1%
Net income	$ 1,599	$ 1,064	-33.5%

* Not meaningful

Operating Revenues

Consolidated operating revenues increased $115 in the first quarter of 2005 compared to the first quarter of 2004. Communications group revenues increased $105 compared to first quarter 2004 reflecting growth in DSL and long distance products partially offset by the impact of revenue declines associated with competitive line losses and related pricing pressures. Revenues from DSL and long distance combined increased $217 in first quarter 2005 compared to first quarter 2004. In addition, first quarter 2004 was negatively affected by a $50 customer refund accrual associated with a settlement agreement with the South

Carolina Consumer Advocate. Revenue trends are discussed in more detail in the Communications group and Advertising & Publishing group segment results sections.

Operating Expenses

Total operating expenses increased $121 in first quarter 2005 compared to the prior year. This increase was primarily driven by increased labor costs of $84, which includes higher expense associated with pension and postretirement benefit plans. As a result of the agreement with the CWA in the third quarter 2004, the increase in contractual limits of the company-funded portion of retiree medical costs (referred to as caps) created a substantive plan that is uncapped and resulted in a significant increase in the benefit obligation. This obligation is currently being recognized over the remaining years of future service to full eligibility of active plan participants. Accordingly, current period expense is higher than the corresponding prior year period in which the benefit obligation was treated as a capped plan. The impact of workforce reductions was substantially offset by annual wage increases. In addition to higher labor costs, costs of goods sold increased $37, primarily for the provision of long distance services associated with the growth in subscribers. First quarter 2005 also included $39 of charges for the Universal Service Fund related to a one-time true up of prior year expense, increases in fund contribution rates and a higher assessment base driven by growth in DSL. Higher depreciation and amortization expense of $20 contributed to the year-over-year increase and was attributable to additional capital spending since first quarter 2004 partially offset by lower depreciation rates. These increases were partially offset by lower uncollectible expense of $17 attributable to continued improvements in economic conditions.

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

Interest Expense

	For the Three Months Ended March 31, 2004	2005	Change
Interest expense - debt	$ 200	$ 263	$ 63
Interest expense - other	15	28	13
Total interest	$ 215	$ 291	$ 76
Average debt balances	$ 13,211	$ 19,562	6,351
Effective rate	6.0%	5.4%	(60) bps

Interest expense increased $76 in first quarter 2005 compared to first quarter 2004. Interest expense associated with interest-bearing debt was up $63 for the first quarter of 2005 compared to the first quarter of 2004 reflecting higher average debt balances impacted by higher incremental borrowings associated with our equity contributions to Cingular to fund its acquisition of AT&T Wireless. The impact of the higher balances was partially offset by lower effective interest rates due to interest rate swaps and refinancing higher-rate debt with lower-rate debt. The change in interest expense-other relates primarily to the reversal of interest accruals in the prior year related to tax contingencies based on audit settlements.

Net earnings (losses) of equity affiliates

	For the Three Months Ended March 31, 2004	2005	Change
Cingular	$ 95	$ (94)	$ (189)
Other equity investees	9	14	5
Total	$ 104	$ (80)	$ (184)

Earnings from Cingular in first quarter 2005 were lower compared to first quarter 2004 primarily due to significant growth in customers and the costs related to that growth, as well as impacts from the AT&T Wireless acquisition, which included integration costs. In addition, depreciation expense was higher in 2005 driven by increased capital investments and a reduction in the useful life of TDMA assets.

Gain (loss) on sale of operations

Gain on sale of operations in first quarter 2004 relates to the sale of our interest in Danish wireless provider, Sonofon, for 3.68 billion Danish Kroner to Telenor ASA. As a result of the sale, we recorded a gain of $462, or $295 net of tax, which included the recognition of cumulative foreign currency translation gains of $13.

Other income (expense), net

	For the Three Months Ended March 31, 2004	2005	Change
Interest income	$ 69	$ 63	$ (6)
Loss on early extinguishment of debt	--	(22)	(22)
Other, net	(5)	15	20
Total Other Income (Expense), net	$ 64	$ 56	$(8)

Provision for income taxes

The provision for income taxes decreased $269 in first quarter 2005 compared to the prior year period while the effective tax rate decreased to 34.1% in first quarter 2005 from 35.1% in first quarter 2004. The lower rate in 2005 was impacted by a year-over-year increase in the benefit associated with the Medicare Part D subsidy which is treated as income for book purposes but is not taxable. In addition, the first quarter of 2005 includes a reduction to deferred income tax liabilities due to a change in state income tax rates. The rate in first quarter 2004 was impacted by the sale of our Denmark operations and a true up of taxes payable associated with divested operations.

Income (loss) from discontinued operations, net of tax

Income (loss) from discontinued operations, net of tax, declined $68 in first quarter 2005 compared to the same period in 2004. In first quarter 2005, we sold the final two of the ten Latin American properties, which resulted in a $390 gain, net of tax. The first quarter 2004 income includes results from operations on all ten properties, as well as a $424 tax benefit related to excess tax basis over book basis in our Latin American investments.

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

Results by Segment

Our reportable segments reflect strategic business units that offer similar products and services and/or serve similar customers. We have three reportable operating segments:

- Communications Group;
- Domestic Wireless; and
- Advertising and Publishing Group.

Management evaluates the performance of each business unit based on net income, exclusive of internal charges for use of intellectual property and adjustments for unusual items that may arise. Unusual items are transactions or events that are included in reported consolidated results but are excluded from segment results due to their nonrecurring or nonoperational nature. In addition, when changes in our business affect the comparability of current versus historical results, we adjust historical operating information to reflect the current business structure. See Note J to our consolidated financial statements for a reconciliation of segment results to the consolidated financial information.

The following discussion highlights our performance in the context of these segments. For a more complete understanding of our industry, the drivers of our business, and our current period results, you should read this discussion in conjunction with our consolidated financial statements, including the related notes.

Communications Group

The Communications Group includes our core domestic businesses including: all domestic wireline voice, data, broadband, e-commerce, long distance, Internet services and advanced voice features. The Communications Group provides these services to an array of customers, including residential, business and wholesale. Beginning in the first quarter 2005, BellSouth began to include various corporate entities, the largest of which is the Information Technology Group, in the Communications Group segment for financial reporting purposes. These entities previously billed their costs to the Communications Group. This change simplifies management reporting, is principally timing in nature and does not affect the consolidated financial statements. Prior period segment operating results were recast to reflect the reporting change.

During first quarter 2005, the Communications Group continued to emphasize interLATA long distance and FastAccess(R) DSL, encouraging customers to purchase packages containing multiple telecommunications services. We also continued to experience retail access line market share loss due to competition and technology substitution, and we expect these overall trends to continue during the remainder of 2005.

	For the Three Months Ended March 31, 2004	2005	Percent Change
Segment operating revenues:			
Voice	$3,169	$3,159	-0.3%
Data	1,091	1,160	6.3%
Other	304	299	-1.6%

Total segment operating revenues	4,564	4,618	1.2%
Segment operating expenses:			
Cost of services and products	1,741	1,853	6.4%
Selling, general, and administrative expenses	745	738	-0.9%
Depreciation and amortization	891	910	2.1%
Total segment operating expenses	3,377	3,501	3.7%
Segment operating income	1,187	1,117	-5.9%
Segment net income	697	664	-4.7%
Segment net income including unusual items	655	650	-0.8%

Key Indicators (000s except where noted)

Switched Access Lines (1):			
Residence Retail:			
Primary	12,200	11,752	-3.7%
Additional	1,525	1,304	-14.5%
Total Retail Residence	13,725	13,056	-4.9%
Residential Wholesale:			
Resale	160	133	-16.9%
UNE-P	1,963	1,886	-3.9%
Total Wholesale Residence	2,123	2,019	-4.9%
Total residence	15,848	15,075	-4.9%

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

Key Indicators (continued)	For the Three Months Ended March 31, 2004	2005	Percent Change
Business Retail	5,354	5,251	-1.9%
Business Wholesale:			
Resale	67	60	-10.4%
UNE-P	714	737	3.2%
Total wholesale business	781	797	2.0%

Total business	6,135	6,048	-1.4%
Other Retail/Wholesale Lines (primarily public)	104	96	-7.7%
Total Switched access lines	22,087	21,219	-3.9%
DSL customers (retail and wholesale)	1,618	2,349	45.2%
Retail long distance customers	4,596	6,470(2)	40.8%
Switched access and local minutes of use (millions)	18,719	16,151	-13.7%
Retail long distance minutes of use	4,574	6,011	31.4%
Total access minutes of use (millions)	23,293	22,162	-4.9%
Capital expenditures	$626	$ 742	18.5%

(1) Prior period operating data are often revised at later dates to reflect updated information. The above information reflects the latest data available for the periods indicated.

(2) Long distance subscribers have been restated to exclude 115,000 toll blocked customers. These non-revenue generating customers have either voluntarily decided to block long distance calling capabilities or have been offered local calling capabilities only due to a lack of credit or billing history.

Segment operating revenues

Communications Group revenues grew 1.2% in the first quarter of 2005 compared to the same quarter of last year, driven by higher DSL and long distance customers and improving access line trends. Revenues from data services increased 6.3 percent in the quarter, while voice revenues were down only 0.3 percent. Other revenue fell 1.6 percent compared to first quarter 2004.

Voice

Voice revenues decreased $10 in the first quarter of 2005 compared to the same period in 2004 driven primarily by continued access line loss partially offset by the growth in interLATA long distance. Total switched access lines declined 868,000, or 3.9%, for the period. The access line decline was the result of continued share loss and technology substitution, primarily wireless.

Wholesale lines, which consist primarily of unbundled network element -- platform (UNE-P) lines, totaled almost 2.9 million at March 31, 2005, down 78,000 lines year over year. When lines over which we provide retail services are converted to UNE-P, we lose revenue and margin. As discussed under the heading "Overview" above, the FCC recently abolished unbundled local switching, the key component of UNE-P. As a result, we have reached commercial agreements with more than 100 of our competitor-customers, placing more than 1.5 million former UNE-P lines under contract at negotiated rates. We believe the change in the regulatory environment influenced the loss of UNE-P lines.

In efforts to combat share loss, we continue to grow our package services. BellSouth Answers(R) is our signature residential package offering, which combines various wireline, wireless, Internet services and/or DIRECTV(R) digital satellite television services. The package combines the Complete Choice calling plan of local service and multiple convenience calling features with BellSouth Long Distance, BellSouth(R) FastAccess(R) DSL or dial-up Internet, and Cingular Wireless services. During 2004, we began offering DIRECTV(R) digital satellite television service through all sales channels as part of the BellSouth Answers(R) portfolio. This agency relationship with DIRECTV(R) provides us with a key competitive product with insignificant cost or capital requirements. With the addition of video, the BellSouth Answers(R) package is one of the most comprehensive and competitively priced bundles in our markets today. We ended first quarter 2005 with over 4.6 million residential packages, representing a 39% penetration of our retail primary line residence base. Almost 85% of Answers customers have long distance in their package and over 45% have either DSL or BellSouth dial-up Internet.

Long distance voice revenue increased $144 in first quarter 2005 when compared to the same period in 2004, driven primarily by growth in interLATA and wireless long distance. InterLATA retail revenues increased $125 reflecting continued large market share gains driven by marketing efforts and the BellSouth Unlimited Long Distance Plans. At March 31, 2005, we had nearly 6.5 million retail long distance customers and a mass-market penetration rate of approximately 50% of our

customer base. We also continued to grow our long distance offerings in complex business. We recorded $31 in complex long distance voice revenue in first quarter 2005 compared to $22 in the same period in 2004. Revenue from wholesale long distance services provided to Cingular increased $15 when compared to first quarter 2004. This increase was caused by higher volumes associated with the proliferation of wireless package plans that include long distance partially offset by slightly lower rates.

Switched access revenues declined $7 in first quarter 2005 when compared to the same period in 2004 due to declines in volumes. Our entry into interLATA long distance shifted switched access minutes from other carriers to our service, resulting in a transfer from wholesale switched access revenues to retail long distance revenue. Excluding our retail long distance traffic, switched access and local minutes of use decreased 13.7% compared to first quarter 2004. The decrease is due to access line losses and alternative communications services, primarily wireless and e-mail.

Data

Data revenues increased $69 in first quarter 2005 when compared to the same period in 2004. Data revenues were driven by strong growth from the sale of BellSouth(R) FastAccess(R) DSL service partially offset by decreases in revenue from other data products. Combined wholesale and retail DSL revenues of $293 were up $79 in first quarter 2005 when compared to first quarter 2004 due primarily to a larger customer base. As of March 31, 2005, we had over 2.3 million DSL customers, an increase of 731,000 customers compared to March 31, 2004.

Retail data services grew 13.8% in first quarter 2005 when compared to the same period in 2004 driven primarily by the growth from the sale of FastAccess DSL service. BellSouth provides tiered DSL speeds and associated pricing to meet a broad range of customer needs. BellSouth(R) FastAccess(R) DSL Ultra runs at downstream connection speeds of up to 1.5 megabits. For customers who want higher speeds, the Company offers BellSouth(R) FastAccess(R) DSL Xtreme, delivering downstream speeds of up to 3.0 megabits and upload speeds of up to

384 kilobits. The Company also offers a lower speed version - BellSouth(R) FastAccess(R) DSL Lite - that runs at downstream speeds of up to 256 kilobits. We set a new record in the first quarter of 2005 with 253,000 DSL net customer additions compared to 156,000 in the first quarter of 2004, a 62 percent growth rate. Competitive promotional offers and reduced churn contributed to customer growth in the first quarter of 2005. Retail DSL customer subscribers grew by 272,000, and were offset by a decline of 19,000 wholesale customers, as AOL completed its exit from offering DSL-based Internet service in January. Revenue from other retail data products was flat for first quarter 2005 when compared to the same period in 2004.

Revenues from the sale of wholesale data transport services and wholesale DSL to other communications providers, including long distance companies and CLECs, declined 2.4% in the first quarter of 2005 when compared to the first quarter of 2004, due to AOL's exit from DSL-based Internet service, which caused approximately half of the decline in wholesale data revenue. The remainder of the decrease was due to declines in data transport sold to inter-exchange carriers that were partially offset by revenue growth in transport sold to wireless carriers.

Other

Other revenues decreased $5 in first quarter 2005 when compared to the same period in 2004 reflecting a decline in revenues from wholesale long distance of $23 due to lower volumes. This decline was substantially offset by increases in equipment revenues of $6 driven by increased demand due to improved economic conditions and customer upgrades to newer technology and increased sales commissions of $10 related to customer additions under our sales agency agreement with DIRECTV.

Segment operating expenses

Cost of services and products

Cost of services and products of $1,853 in first quarter 2005 increased $112 from first quarter 2004. The increase included $55 in labor due primarily to increases in retiree medical costs and anuual wage increases, offset by workforce reductions; $39 related to Universal Service Fund contributions related to a one-time true up of prior year expense, increases in fund contribution rates and a higher assessment base driven by growth in DSL; $37 in costs of goods sold principally driven by higher volumes in long distance services; and $20 in materials and supplies driven primarily by DSL modem cost associated with customer growth. These increases were partially offset by a $17 decline in access fees in the first quarter 2005 due to lower volumes.

Selling, general, and administrative expenses

Selling, general, and administrative expenses of $738 in first quarter 2005 decreased $7 from first quarter 2004. This decrease reflects lower uncollectibles expense of $26 driven by lower receivable write-offs attributable to continued improvements in economic conditions. This decrease was partially offset by an increase of $17 in labor costs driven by retiree medical benefits and annual wage increases.

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

Depreciation and amortization

Depreciation and amortization expense increased $19 during first quarter 2005 when compared to the same period in 2004 reflecting increased capital spending, partially offset by reduced depreciation rates under the group life method of depreciation.

Unusual items excluded from segment net income

Unusual items that were excluded from this segment's net income consisted of the following: for first quarter 2005, unusual items of $14 for the early extinguishment of debt; for first quarter 2004, unusual items of $42 for the South Carolina regulatory settlement and severance.

Domestic Wireless

We own an approximate 40 percent economic interest in Cingular, a joint venture with SBC Communications. Because we exercise influence over the financial and operating policies of Cingular, we use the equity method of accounting for this investment. Under the equity method of accounting, we record our proportionate share of Cingular's earnings in our consolidated statements of income. These earnings are included in the caption "Net earnings (losses) of equity affiliates." For management purposes, we evaluate our Domestic wireless segment based on our proportionate share of Cingular's results. Accordingly, results for our Domestic wireless segment reflect the proportional consolidation of approximately 40 percent of Cingular's results and taxes at the parent level, excluding unusual items.

On October 26, 2004, Cingular completed the acquisition of AT&T Wireless, creating the largest wireless carrier in the United States based on revenues and number of customers. The wireless industry continued its strong growth trajectory during the first quarter of 2005. Despite continued industry consolidation, competition continues to be intense, with five national competitors. On a pro forma basis, Cingular's average revenue per user (ARPU) declined 3.3 percent from first quarter 2004 to first quarter 2005, driven primarily by lower revenue derived from voice services partially offset by increased data-related revenues. Data revenue played an increasingly important role in revenue composition in 2004 and early 2005, and those impacts are expected to increase through the remainder of 2005.

In the first quarter of 2005, to be consistent with industry practices, Cingular's income statement presentation was changed for the current and prior-year periods to reflect, as revenues, the gross receipts tax and other fees billed to customers and to reflect, as expenses, the taxes assessed by the various state jurisdictions. The impact of this reclassification was an increase in first-quarter revenue and expense of $16 for BellSouth's 40 percent share reported in our wireless segment. Similar revenue and expense increases for the same quarter a year ago were $10. Operating income and net income for all periods were unaffected by this reclassification in income statement presentation.

	For the Three Months Ended March 31, 2004	2005	Percent Change
Segment operating revenues:			
Service revenues	$ 1,433	$2,968	107.1%
Equipment revenues	154	324	110.4%
Total segment operating revenues	1,587	3,292	107.4%
Segment operating expenses:			
Cost of services and products	594	1,375	131.5%
Selling, general, and administrative expenses	548	1,159	111.5%
Depreciation and amortization	221	670	203.2%

Total segment operating expenses	1,363	3,204	135.1%
Segment operating income	224	88	-60.7%
Segment net income (loss)	$ 59	$ (33)	-155.9%
Segment net income (loss) including unusual items	$ 59	$ (54)	-191.5%
Key Indicators (100% Cingular):			
Cellular/PCS Customers (000s)	24,618	50,369	104.6%
Wireless service average monthly revenue per customer - Cellular/PCS	$ 48.30	$49.59	2.7%
Capital Expenditures	$ 334	$ 971	190.7%

Segment operating revenues

During the first quarter 2005, Cingular had net additions of 1.4 million customers, resulting in 50.4 million cellular/PCS customers on March 31, 2005. This represents a growth of 25.8 million in Cingular's cellular/PCS customer base from a year ago, including approximately 22 million customers Cingular assumed in its acquisition of AT&T Wireless. Postpaid gross additions were 76% of all gross additions, up from 71% in 2004.

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

The first quarter cellular/PCS churn rate was 2.2%, down from a 2.7% churn rate in the same period a year ago. Approximately 10 basis points of the reduction in Cingular's churn rate resulted from operational improvement. The remaining reduction in churn is attributable to Cingular's adoption of a new reseller churn calculation methodology that is more comparable with its major competitors and changes to conform churn calculation methodologies of Cingular and AT&T Wireless.

Segment operating revenue grew $1,705 during the first quarter of 2005 as compared to the same period of 2004 primarily as a result of the increased revenue associated with Cingular's acquisition of AT&T Wireless in fourth quarter of 2004. Wireless service revenue increased $1,535 quarter-over-quarter primarily as a result of the AT&T Wireless acquisition. ARPU increased 2.7% to $49.59 in the first quarter, up from $48.30 in the prior year quarter. Higher ARPU was driven by higher customer usage and increased per unit contribution from data services and increases in long distance and regulatory fee revenues. Additionally, ARPU for the first quarter of 2005 reflects the ARPU of the acquired AT&T Wireless customer base which in general had higher ARPUs than the traditional Cingular customer base. Partially offsetting these increases was a decline in the per user contribution from Cingular's monthly access charges and airtime usage. Declines in per unit access and airtime charges were driven by an increase in the number of customers on RollOver plans and also due to free mobile to mobile minutes, which allow Cingular customers to call other Cingular customers at no charge. Additionally, per unit access and airtime charges decreased due to a larger embedded customer base on lower ARPU rate plans, including FamilyTalk(R), more customers sold through resellers, and rate plans that include larger buckets of minutes, thereby reducing billed minute overages.

Equipment sales contributed $170 of the increase in total operating revenue, driven primarily by incremental revenue from higher unit sales reflecting a 90.7% increase in gross customer additions and increased upgrade sales as Cingular migrated former AT&T Wireless customers to Cingular rate plans. Partially offsetting this growth was an overall decline in the average revenue per unit sold.

Segment operating expenses

Cost of services and products

Cost of services and products of $1,375 in first quarter 2005 increased $781 when compared to the same 2004 period. Cingular's systems expense growth was driven by increased local network system costs associated with the acquired AT&T Wireless network, including higher interconnection fees associated with a 133.8% growth in system minutes of use; higher facilities related costs resulting from the increase in cell sites and with maintaining additional duplicate TDMA and GSM networks; and increased USF and regulatory fees from the increase in the customer base and rate changes. Local network system cost also increased as a result of the termination of Cingular's joint venture with T-Mobile, GSMF. Additionally, higher equipment-related expenses quarter-over-quarter were driven by increased gross additions and upgrade activity, partially offset by a decline in the average cost per unit sold.

Selling, general, and administrative expenses

Selling, general, and administrative expenses of $1,159 in first quarter 2005 increased $611 when compared to first quarter 2004. The growth was primarily due to the incremental expenses associated with the recently acquired AT&T Wireless markets. Additionally, growth was also driven by volume through higher advertising and promotions expenses, increased commissions expenses related to the 90.7% increase in gross customer additions, an increase in upgrade commissions, an increase in billing expenses, and expenses related to customer retention and customer service improvement initiatives.

Depreciation and amortization

Depreciation and amortization increased $449 in first quarter 2005 when compared to the same period in 2004. Depreciation expense for the first quarter of 2005 increased primarily due to incremental depreciation associated with the property, plant and equipment acquired from the AT&T Wireless acquisition and depreciation related to Cingular's on-going capital spending associated with its GSM network. Additionally, depreciation expense increased over the prior year period as a result of a reduction of the useful lives of certain TDMA and other equipment, which increased BellSouth's share of depreciation expense by approximately $40 during the first quarter of 2005. Intangibles amortization expense for the first quarter of 2005 increased from the same period in 2004 primarily related to the purchase price valuation of customer contracts acquired through the AT&T Wireless acquisition. This increase was partially offset by certain historical Cingular finite-lived intangible assets becoming fully amortized during 2004.

Unusual items excluded from segment net income

Unusual items that were excluded from this segment's net income consisted of the following: for first quarter 2005, unusual items of $21 for wireless merger integration costs. There were no unusual items excluded from first quarter 2004.

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

Advertising and Publishing Group

Our Advertising and Publishing Group is comprised of companies in the US that publish, print, and sell advertising in and perform related services concerning alphabetical and classified telephone directories and electronic media offerings.

In the first quarter of 2005, our Advertising and Publishing Group continued to see the favorable impact from strategic initiatives implemented in 2004 and from an improving economy, offset by continued competitive pressures.

	For the Three Months Ended March 31, 2004	2005	Percent Change
Segment operating revenues	$ 482	$491	1.9%
Segment operating expenses:			
Cost of services and products	80	90	12.5%
Selling, general, and administrative expenses	156	163	4.5%
Depreciation and amortization	7	7	--
Total segment operating expenses	243	260	7.0%
Segment operating income	239	231	-3.3%
Segment net income	$147	$ 141	-4.1%
Segment net income (loss) including unusual items	$147	$ 141	-4.1%
Capital Expenditures	$8	$ 9	12.5%

Segment operating revenues

Segment operating revenues increased $9 from first quarter 2004 to first quarter 2005. The increase includes an improvement in print revenues as a result of selling effectiveness and new products, and growing electronic media revenues.

Segment operating expenses

Cost of services and products increased $10 from first quarter 2004 to first quarter 2005, primarily reflecting the impact of increased distribution volumes. Selling, general, and administrative expenses increased $7 between periods, primarily driven by increases in employee healthcare, pension and post-retirement medical costs. Variable costs associated with selling also increased as a result of higher revenues. Partially offsetting these increases was a decline in uncollectible expense. The decrease reflects the impact of improved collection performance between periods. Depreciation and amortization expenses were flat between periods.

Unusual items excluded from segment net income

There were no unusual items excluded from this segment's net income.

Liquidity and Financial Condition

Net cash provided by (used for):

	For the Three Months Ended March 31, 2004	2005	Change	
Continuing Operations				
Operating activities...	$ 1,728	$ 1,718	(10)	-0.6%
Investing activities...	$ (395)	$ 560	955	*
Financing activities...	$ (778)	$ (2,327)	(1,549)	*
Discontinued Operations	$ (9)	$ (115)	(106)	*

*Not meaningful.

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

CONTINUING OPERATIONS

Net cash provided by operating activities

Cash generated by operations decreased $10 during first quarter 2005 compared to the prior year period. Operating income before depreciation and amortization expense in the first quarter of 2005 was comparable to the first quarter of 2004. The decline in cash flows from operations was driven by higher interest payments substantially offset by lower tax payments in first quarter 2005 as compared to the first quarter of 2004.

Net cash used for investing activities

Capital expenditures

Capital expenditures consist primarily of (a) gross additions to property, plant and equipment having an estimated service life of one year or more, plus incidental costs of preparing the asset for its intended use, and (b) gross additions to capitalized software. Our capital expenditures during first quarter 2005 of $750 and first quarter 2004 of $635 were incurred to support our wireline network, to promote the introduction of new products and services and to increase operating efficiency and productivity. The increase in capital expenditures compared to the prior period relates primarily to the timing of increased spending on broadband initiatives to meet increasing demand.

Other investing activities

During first quarter 2005, we received $919 in net proceeds from the sale of our Latin American operations and $400 in repayments from Cingular on a revolving line of credit.

During first quarter 2004, we received $525 for the sale of our investment in Sonofon and $109 for the repayment of our shareholder loan and accrued interest, reduced by a settlement of $17 associated with currency swap contracts. In addition, we purchased and sold equity securities for a net cash expenditure of $106 and purchased and sold short-term investments for a net cash expenditure of $266.

Net cash used for financing activities

During first quarter 2005, we utilized cash from operations, sales proceeds, and proceeds from debt issued in the fourth quarter 2004 to reduce short-term borrowings by $1,093, pay down long-term debt by $669, and pay dividends of 27 cents per share totaling $494. In addition, we purchased 3 million shares of our common stock for $77.

During first quarter 2004, we utilized cash from operations to reduce short-term borrowings by $362 and pay dividends of 25 cents per share totaling $457.

DISCONTINUED OPERATIONS

The following table represents cash flows from our discontinued operations:

	For the Three Months Ended March 31, 2004	2005
Operating activities.........	$ 69	$ 10
Investing activities.........	$ (47)	$ (125)
Financing activities.........	$ (31)	$ --
Total cash flows from discontinued operations.....	$ (9)	$ (115)

In first quarter 2005, we purchased $125 of third party Argentine debt in connection with the sale of our Latin American properties.

In first quarter 2004, capital expenditures were $66. Distributions to minority partners of $41 are included in first quarter 2004, offset by net proceeds of $19 related to the purchase and sale of equity securities and $10 for net debt borrowings and repayments.

Anticipated sources and uses of funds

General

The Communications Group and Advertising & Publishing Group generate substantially all of our consolidated cash provided by operating activities. These segments generate sufficient cash flow to fund their investing and financing activities. Should other investing opportunities arise, we believe we are well positioned to raise capital in the public debt markets.

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

The objective of our Board of Directors is to maintain a competitive dividend. They evaluate the cash dividend on a quarterly basis and make decisions regarding the dividend within the context of long-term free cash flow projections.

At March 31, 2005, our long-term debt rating was A2 from Moody's Investor Service and A from Standard and Poor's. Our short-term debt rating at March 31, 2005 was P-1 from Moody's and A-1 from Standard and Poor's. Moody's outlook on both our short and long-term ratings remains negative. The reasons cited were our expanded competitive challenges in the wireline business which could erode our ability to reduce debt levels as planned and the possibility of lower earnings and cash flow at Cingular if the AT&T Wireless integration is more expensive and time consuming than anticipated. Standard and Poor's also has a negative outlook on our long-term debt rating. The reasons given are increasing competition in our wireline business from the cable television companies, which could drive down pricing and squeeze operating margins, and near term pressures from the integration of AT&T Wireless.

Our authorized commercial paper program as of March 31, 2005 was $10.5 billion, with $2.2 billion outstanding. We believe that we have ready access to the commercial paper market in the event funding in excess of our operating cash flows is needed. We also have a registration statement on file with the SEC under which $3.1 billion of long-term debt securities could be issued. Our sources of funds -- primarily from operations and, to the extent necessary, from readily available external financing arrangements -- are sufficient to meet all current obligations on a timely basis. We believe that these sources of funds will be sufficient to meet the operating needs of our business for at least the next twelve months.

Domestic Wireless

BellSouth and SBC provide unsubordinated short-term financing on a pro rata basis for Cingular's ordinary course of business cash requirements based upon Cingular's budgeted and forecasted cash needs. Cingular has terminated its bank credit facilities and no longer issues commercial paper or long-term debt. As of March 31, 2005, we had advances to Cingular, including interest, under the line of credit of $271.

Cash management

BellSouth's primary source of cash flow is dividends from its subsidiaries. Generally, we do not permit our subsidiaries to accumulate cash, requiring them to pay out either net income or cash flow available in the form of dividends. Any funding requirements for wholly owned domestic subsidiaries are fulfilled by BellSouth Corporation.

Debt instruments

BellSouth and BellSouth Telecommunications currently have debt outstanding under various indentures that we have entered into over the past twelve years. None of these indentures contain any financial covenants. They do contain limitations that restrict the Company's (or the affiliate of the company that is a party to the indenture) ability to create liens on their properties or assets (but not the properties or assets of their subsidiaries) except in specified circumstances. None of these indentures contains any provisions that are tied to the ratings assigned to the company or its affiliates by an external debt rating agency. Further, none of these indentures contains cross-default provisions.

On October 4, 2004, we entered into a syndicated credit agreement that provided for lender commitments in the aggregate principal amount of $9.0 billion. As of March 31, 2005, lender commitments under the agreement had been reduced to approximately $2.0 billion. In addition, we had a syndicated line of credit in the amount of $1.5 billion. Both the syndicated credit agreement and the syndicated line of credit served as backup facilities for our commercial paper program. The syndicated line of credit expired on April 29, 2005. Effective April 29, 2005, we entered into a new syndicated line of credit in the amount of $3.0 billion, and we terminated the remaining $2.0 billion lender commitments under the October 4, 2004 credit agreement. The new $3.0 billion line of credit will expire on April 29, 2008.

Except as described in this paragraph, the syndicated line of credit contains no financial covenants or requirements for compensating balances. Further, the line of credit does not contain any provisions that are tied to the ratings assigned to us or our affiliates by an external debt rating agency. The line of credit provides that the debt of the Company and its consolidated subsidiaries is not permitted to exceed 300% of consolidated earnings before interest, taxes, depreciation and amortization for the preceding four quarters. In addition, the line of credit prohibits the Company and its significant subsidiaries from permitting liens to be placed on their properties or assets except in specified circumstances. If BellSouth or any of our subsidiaries defaults on any outstanding debt in excess of $200, an event of default will occur under the line of credit.

(Dollars in Millions, Except Per Share Amounts and as Otherwise Indicated)

Market Risk

For a complete discussion of our market risks, you should refer to the caption "Quantitative and Qualitative Disclosure About Market Risk" in our annual report on Form 10-K for the year ended December 31, 2004. Our primary exposure to market risks relates to unfavorable movements in interest rates. We do not anticipate any significant changes in our objectives and strategies with respect to managing such exposures.

In order to limit our risk from fluctuations in interest rates, we enter into interest rate swap agreements to exchange fixed and variable rate interest payment obligations without the exchange of the underlying principal amounts. In the first quarter of 2005, we entered into an additional interest rate swap, bringing the total notional value of our fair value hedges to $1,500 as of March 31, 2005. Subsequent to the first quarter of 2005, we entered into an additional fair value interest rate swap with a notional value of $100.

Off-Balance Sheet Arrangements and Aggregate Contractual Obligations

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Other than as set forth below, there are no material changes with respect to off-balance sheet arrangements and aggregate contractual obligations as presented in our annual report on Form 10-K for the year ended December 31, 2004.

In most of our sale and divestiture transactions we indemnify the purchaser for various items including labor and general litigation as well as certain tax matters. Generally, the terms last one to five years for general and specific indemnities and for the statutory review periods for tax matters. The events or circumstances that would require us to perform under the indemnity are transaction and circumstance specific. We regularly evaluate the probability of having to incur costs associated with these indemnifications and have accrued for expected losses that are probable. In addition, in the normal course of business, we indemnify counter parties in certain agreements. The nature and terms of these indemnities vary by transaction. Historically, we have not incurred significant costs related to performance under these types of indemnities.

We do not have transactions, arrangements or relationships with "special purpose" entities, and we do not have any off-balance sheet debt.

Operating Environment

Economic Trends

Real gross domestic product (GDP), which increased at an average annual rate of 3.8 percent in the fourth quarter of 2004, grew 4.4 percent in 2004, the best growth since 1999. Real personal consumption growth was at an annual rate of 4.2 percent in the fourth quarter and 3.8 percent for 2004. Fixed investment spending by businesses accelerated to an annual rate of 14.5 percent in the fourth quarter. It was up 10.6 percent for the year overall. Residential fixed investment spending was also strong in 2004, growing 9.6 percent. Real GDP growth was reduced by an increase in imports throughout the year. Economic growth decelerated to an annual rate of 3.1 percent in the first quarter, according to the advance estimate of first quarter GDP. Personal consumption and business fixed investment increased at a more modest pace and imports continued to grow strongly. Employment growth, slow earlier in the year, improved in the fourth quarter of 2004 and in the first quarter of 2005. The economy added 2.2 million jobs in 2004, the best job growth since 1999. The nation's unemployment rate at the end of the first quarter of 2005 was 5.2 percent, down from 5.4 percent in the fourth quarter of 2004. The GDP deflator, a broad measure of inflation, increased at an annual rate of 2.3 percent in the fourth quarter, lifting inflation for the year to 2.2 percent. Concerned with inflation, the Federal Reserve raised short-term interest rates during the second half of 2004 and first quarter of 2005 and will likely continue to raise rates throughout 2005. The economy is expected to expand at a more modest, but still healthy, pace in 2005.

On average, the economy of the nine-state region tends to closely track the US economy. Paced by Florida, growth rates have tended to be faster in the South Atlantic states. The region has experienced strong net migration for several years, a trend that is likely to be sustained. Residential construction activity has been strong as a result. Housing starts surged in 2004, reaching 592,000, easily exceeding 2003's robust level of 533,000. Microsoft's dividend payout boosted the region's real personal income growth to an annual rate of 7.9 percent during the fourth quarter and 3.7 percent for 2004 overall. Employment in the region in the fourth quarter grew at an annual rate of 1.4 percent. It was up 1.7 percent for the year overall. The region's unemployment rate was 5.2 percent in the fourth quarter of 2004. The disruption to economic activity that was caused by four hurricanes that hit the region in 2004 was concentrated in, although not confined to, Florida's economy, the largest in the region. Rebuilding continues early in 2005. The region's economy is expected to expand at a moderate pace in 2005.

Legal Matters

We are involved in numerous legal proceedings associated with state and federal regulatory matters. While complete assurance cannot be given as to the outcome of these matters, we believe that any financial impact would not be material, individually or in the aggregate, to our results of operations, financial position or cash flows. See Note L to our consolidated interim financial statements.

Item 3. Qualitative and Quantitative Disclosures About Market Risk

See the caption labeled "Market Risk" in Management's Discussion and Analysis of Financial Condition and Results of Operations.

Item 4. Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the management, including the Chief Executive Officer and Chief Financial

Officer, as appropriate, to allow timely decisions regarding required disclosure. Management necessarily applied its judgment in assessing the costs and benefits of such controls and procedures, which, by their nature, can provide only reasonable assurance regarding management's control objectives. We also have investments in certain unconsolidated entities. As we do not control or manage these entities, our disclosure controls and procedures with respect to such entities are necessarily more limited than those we maintain with respect to our consolidated subsidiaries.

The Company's management, including the Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls can prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. There are inherent limitations in all control systems, including the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of one or more persons. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and, while our disclosure controls and procedures are designed to be effective under circumstances where they should reasonably be expected to operate effectively, there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Because of the inherent limitations in any control system, misstatements due to error or fraud may occur and not be detected.

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of management, including the Chief Executive Officer along with the Chief Financial Officer, of the effectiveness, of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rules 13a-15(b) and 15d-15(b). Based upon the foregoing, the Chief Executive Officer along with the Chief Financial Officer concluded that our disclosure controls and procedures are effective at providing reasonable assurance that all material information relating to BellSouth (including consolidated subsidiaries) required to be included in our Exchange Act reports is reported in a timely manner. In addition, based on such evaluation we have identified no change in our internal control over financial reporting that occurred during the fiscal quarter covered by this report that has materially affected or is reasonably likely to materially affect, our internal control over financial reporting.

Cautionary Language Concerning Forward-Looking Statements

In addition to historical information, this document contains forward-looking statements regarding events, financial trends and critical accounting policies that may affect our future operating results, financial position and cash flows. These statements are based on our assumptions and estimates and are subject to risks and uncertainties. For these statements, we claim the protection of the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995.

There are possible developments that could cause our actual results to differ materially from those forecast or implied in the forward-looking statements. You are cautioned not to place undue reliance on these forward-looking statements, which are current only as of the date of this filing. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

While the below list of cautionary statements is not exhaustive, some factors, in addition to those contained throughout this document, that could affect future operating results, financial position and cash flows and could cause actual results to differ materially from those expressed in the forward-looking statements are:

- a change in economic conditions in the markets where we operate or have material investments which could affect demand for our services;
- the impact and the success of Cingular Wireless, our wireless joint venture with SBC, including marketing and product development efforts, technological changes and financial capacity;
- Cingular Wireless' failure to realize, in the amounts and within the timeframe contemplated, the capital and expense synergies and other financial benefits expected from its acquisition of AT&T Wireless as a result of technical, logistical, regulatory and other factors;
- changes in laws or regulations, or in their interpretations, which could result in the loss, or reduction in value, of our licenses, concessions or markets, or in an increase in competition, compliance costs or capital expenditures;
- continued pressures on the telecommunications industry from a financial, competitive and regulatory perspective;
- the intensity of competitive activity and its resulting impact on pricing strategies and new product offerings;
- changes in the federal and state regulations governing the terms on which we offer retail and wholesale services;
- continued successful penetration of the interLATA long distance market;
- the impact on our business of consolidation in the wireline and wireless industries in which we operate;
- the issuance by the Financial Accounting Standards Board or other accounting bodies of new accounting standards or changes to existing standards;
- changes in available technology that increase the impacts of technology substitution;
- higher than anticipated start-up costs or significant up-front investments associated with new business initiatives;
- the outcome of pending litigation; and
- unanticipated higher capital spending from, or delays in, the deployment of new technologies.

PART II -- OTHER INFORMATION

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The following table contains information about our purchases of our equity securities during the first quarter of 2005.

Issuer Purchases of Equity Securities

	Total Number	Average	Total Number of Shares Purchased as Part of a	Approximate Dollar Value that May Yet Be

Period	of Shares Purchased (1)	Price Paid per Share	Publicly Announced Plan	Purchased Under the Plan
January 1-31, 2005	1,202	$26.78	--	--
February 1-28, 2005	--	--	--	--
March 1-31, 2005	3,139,174	$26.21	--	--
Total	3,140,376	$26.21	--	--

(1) Represents 191,276 shares purchased from employees to pay taxes related to the vesting of restricted shares, at an average price of $26.03, and 2,949,100 shares purchased from the external markets at an average price of $26.22. Excludes shares purchased from employees to pay taxes related to the exercise of stock options.

Item 6. Exhibits

Exhibit Number	
4a	No instrument which defines the rights of holders of our long- and intermediate-term debt is filed herewith pursuant to Regulation S-K, Item 601(b)(4)(iii)(A). Pursuant to this regulation, we agree to furnish a copy of any such instrument to the SEC upon request.
10bbb	Form of 2005 Ownership Restricted Stock Award Agreement pursuant to BellSouth Executive Stock Ownership Program.
11	Computation of Earnings Per Common Share.
12	Computation of Ratio of Earnings to Fixed Charges.
31a	Section 302 certification of F. Duane Ackerman.
31b	Section 302 certification of Ronald M. Dykes.
32	Statement Required by 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURE

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

BELLSOUTH CORPORATION

By /s/ Pat Shannon
PAT SHANNON
Senior Vice President - Finance and Controller
(Principal Accounting Officer)

May 4, 2005

EXHIBIT INDEX

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