

**WASHINGTON 534 & 530
INLAND TELEPHONE COMPANY**
(A Wholly-Owned Subsidiary of
Western Elite Incorporated Services)

Audited Financial Statements

December 31, 2009 and 2008

WASHINGTON 534 & 530
INLAND TELEPHONE COMPANY
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Western Elite Incorporated Services)

Audited Financial Statements

December 31, 2009 and 2008

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1501 Regents Blvd., Suite 100

Fircrest, WA 98466

(253)566-7070

fax (253)566-7100

Independent Auditor's Report

Board of Directors
Inland Telephone Company
Roslyn, Washington

We have audited the accompanying balance sheets of Inland Telephone Company (a wholly-owned subsidiary of Western Elite Incorporated Services) as of December 31, 2009 and 2008, and the related statements of income, stockholder's equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Inland Telephone Company as of December 31, 2009 and 2008, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated April 9, 2010, on our consideration of Inland Telephone Company's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

Johnson, Stone & Pagano, P.S.
JOHNSON, STONE & PAGANO, P.S.

April 9, 2010

AUDITED FINANCIAL STATEMENTS

**WASHINGTON 534 & 530
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BALANCE SHEETS

December 31, 2009 and 2008

2009

2008

ASSETS

REDACTED

See accompanying notes to financial statements.

2009

2008

LIABILITIES AND STOCKHOLDER'S EQUITY

REDACTED

**WASHINGTON 534 & 530
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STATEMENTS OF INCOME

Years Ended December 31, 2009 and 2008

2009

2008

REDACTED

See accompanying notes to financial statements.

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STATEMENTS OF STOCKHOLDER'S EQUITY

Years Ended December 31, 2009 and 2008

<u>Common Stock</u>	<u>Additional Paid-in Capital</u>	<u>Retained Earnings</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>	<u>Total</u>
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REDACTED

See accompanying notes to financial statements.

**WASHINGTON 534 & 530
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STATEMENTS OF CASH FLOWS

Years Ended December 31, 2009 and 2008

2009

2008

CASH FLOWS FROM OPERATING ACTIVITIES

REDACTED

See accompanying notes to financial statements.

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STATEMENTS OF CASH FLOWS (Continued)

Years Ended December 31, 2009 and 2008

**COMPONENTS OF NET CHANGE IN OPERATING
ASSETS AND LIABILITIES**

2009

2008

REDACTED

See accompanying notes to financial statements.

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

**NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES**

Telephone Industry

Inland Telephone Company (“Company”) is a local exchange telecommunications company providing local exchange and other telecommunications services to customers in Columbia, Kittitas, Mason, Whitman and Walla Walla counties in Washington, and Latah and Nez Perce counties in Idaho.

Regulatory changes in the telecommunications industry have modified, or could modify, the manner in which the Company's approved telecommunication tariffed rates are calculated as well as modify the manner in which the Company recovers its revenue requirements. Implementation of these modifications and the outcome of regulatory proceedings may adversely affect certain current or future revenue streams of the Company.

Organization

The Company is a wholly-owned subsidiary of Western Elite Incorporated Services.

Regulation

The Company is subject to the accounting rules and rate regulation policies of the Washington Utilities and Transportation Commission (“WUTC”) and the Idaho Public Utilities Commission (“IPUC”) and adheres to the Federal Communications Commission (“FCC”) Uniform System of Accounts for a Class B telephone company as prescribed by the FCC under Part 32.

Cash

For purposes of the statements of cash flows, the Company considers cash to be cash on hand, in checking accounts and in money market accounts.

Investment in Corporations

The Company uses the cost method of accounting for investments in corporations, unless fair market value is readily determinable.

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

**NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES (Continued)**

Fair Value Measurements

On January 1, 2009, the Company adopted applicable authoritative guidance related to fair value measurements that defines fair value, provides a framework to measure the fair value of assets and liabilities and requires certain disclosures about those measurements. The guidance establishes a hierarchy to prioritize the inputs that underlie a fair value measurement and requires that valuation techniques maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs essentially distinguish the relative reliability of inputs to fair value measurements. Level 1 inputs are more reliable and objective than Level 2 inputs which are in turn more reliable and objective than Level 3 inputs. In arriving at a fair value measure, the Company is required to determine the level in the fair value hierarchy within which a fair value measurement ultimately falls and provide disclosure of such determinations.

Telecommunications Plant

Telecommunications plant is stated at cost and is depreciated on a straight-line basis for accounting purposes. Lives used for calculating depreciation on telecommunications plant are in accordance with the rules of the WUTC and IPUC and are based on the estimated economic useful lives of the assets.

Telecommunications Plant Retirements

When an asset is retired or otherwise disposed of, the cost of the asset is removed from the asset account and charged to the related allowance for depreciation. Similarly, the cost of removal and salvage proceeds are charged or credited to the allowances for depreciation. Consequently, no gain or loss upon disposition is recognized.

Allowance for Funds Used During Construction

Interest applicable to funds used for long-term construction projects is capitalized as a part of the cost of the asset and depreciated over the asset's estimated useful life. **REDACTED**

REDACTED

Advertising Costs

Costs incurred for advertising are expensed as incurred. Advertising expense was **REDACTED** **REDACTED** for the years ended December 31, 2009 and 2008, respectively.

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

**NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES (Continued)**

Revenue Recognition, Major Customers and Services

Services provided by the Company include primarily local network and network access services. Network access service revenues, which represent a major portion of the Company's operating revenues, are derived from the provision of exchange access services to interexchange carriers or to end users of telecommunication services beyond the Company's local network.

Revenues for interstate access services are received through tariffed access charges filed by the National Exchange Carrier Association ("NECA") with the FCC on behalf of the NECA member companies. These access charges are billed by the Company to interstate interexchange carriers and pooled with like-revenues from all NECA member companies. The pooled access charge revenues received by the Company are based upon the actual cost of providing interstate access services, plus a return on the investment dedicated to providing these services. Pooled access charge revenues are estimated at December 31 each year and are subject to adjustment. Such adjustments are normal occurrences and are recorded by the Company during the year in which they occur.

Revenues for Washington State intrastate access services are received through tariffed access charges filed by the Company and the Washington Exchange Carrier Association ("WECA") and approved by the WUTC. The access charges are billed by the Company to intrastate interexchange carriers. The carrier common line and state universal service fund revenues are pooled with all WECA member companies. The traffic sensitive revenues are considered bill and keep based on tariffed rates.

Revenues for Idaho State intrastate access services are received through tariffed access charges filed by the Company and approved by the IPUC. The access charges are billed by the Company to intrastate interexchange carriers and are considered bill and keep based on tariffed rates.

For some of the services that the Company provides to its customers, the Company relies upon services and facilities supplied to it by other companies. Any material disruption of the services or facilities supplied to the Company by other companies could potentially have an adverse effect upon the Company's operating results.

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

**NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES (Continued)**

Federal and State Income Taxes



Comprehensive Income

Authoritative guidance requires that total comprehensive income be reported in the financial statements. Total comprehensive income is presented on the statements of stockholder's equity.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates and assumptions used in preparing the accompanying financial statements.

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

**NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT
ACCOUNTING POLICIES (Continued)**

Subsequent Events

The management of the Company evaluated for subsequent events and transactions for potential recognition and disclosure through April 9, 2010 the date the financial statements were available to be issued. No such subsequent events were noted.

NOTE 2 - CONCENTRATION OF CREDIT RISK

The Company maintains cash balances at various financial institutions in eastern Washington. Accounts at each of the financial institutions are insured by the Federal Deposit Insurance Corporation ("FDIC") with basic coverage up to \$250,000 until December 31, 2013. The Company's non-interest bearing accounts have unlimited FDIC deposit insurance through June 30, 2010. At December 31, 2009, the Company's cash balances at the institutions did not exceed the FDIC insured amount.

REDACTED

The Company's accounts receivable are subject to potential credit risk as they are unsecured.

NOTE 3 - TELECOMMUNICATIONS ACCOUNTS RECEIVABLE

The telecommunications accounts receivable balance consists of:

	<u>2009</u>	<u>2008</u>
Due from customers and agents		
Due from exchange carriers and exchange carrier associations		
Other accounts receivable		
Allowances for doubtful accounts (deduction)		

REDACTED

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

NOTE 3 - TELECOMMUNICATIONS ACCOUNTS RECEIVABLE (Continued)

The Company extends credit to its business and residential customers based upon a written credit policy. Service interruption is the primary vehicle for controlling losses. Telecommunications accounts receivable are recorded when subscriber bills, carrier access bills, and exchange carrier associations settlement statements are billed and are presented in the balance sheets net of the allowance for doubtful accounts. Certain exchange carrier associations' settlements are subject to out-of-period adjustments and are recorded during the year in which they become determinable. The allowance for doubtful accounts is estimated based on the Company's historical losses, the existing economic conditions in the telecommunications industry, and the financial stability of its customers. At December 31,

REDACTED

NOTE 4 - INVESTMENT IN CORPORATIONS

Investments consist of the following:

Investment in Corporations

2009

2008

REDACTED

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

NOTE 4 - INVESTMENTS IN STOCKS AND PARTNERSHIP (Continued)

As described in Note 1, the Company has adopted applicable authoritative guidance related to fair value measurements. Following is the hierarchy and fair value measurements at December 31, 2009 and 2008:

REDACTED

Investments valued using Level 1 inputs are based on unadjusted quoted market prices within active markets. Investments valued using Level 2 inputs are based primarily on quoted prices for similar assets in active or inactive markets. Level 3 inputs are based on the Company's own assumptions on how knowledgeable parties would price assets or liabilities, and are developed using the best information available in the circumstances.

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

NOTE 5 - TELECOMMUNICATIONS PLANT IN SERVICE AND DEPRECIATION

Telecommunications plant in service is stated at cost. Listed below are the major classes of the telecommunications plant:

	<u>2009</u>	<u>2008</u>
General support facilities	REDACTED	
Central office equipment		
Cable and wire facilities		
Intangible assets		

Provisions have been made for depreciation of major classes of the telecommunications plant at straight-line rates as follows:

General support facilities		
Buildings	2.50%	- 4.00%
Furniture and office equipment	15.00%	- 25.00%
Vehicles and other work equipment	12.50%	- 16.00%
Central office equipment	9.00%	- 11.19%
Cable and wire facilities	5.00%	- 42.06%

NOTE 6 - LONG-TERM DEBT

REDACTED

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

NOTE 6 - LONG-TERM DEBT (Continued)

REDACTED

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NOTES TO FINANCIAL STATEMENTS

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NOTE 6 - LONG-TERM DEBT (Continued)

REDACTED

NOTE 7 - FEDERAL AND STATE INCOME TAXES

The Company recognizes deferred income taxes for differences between the basis of assets and liabilities for financial statement and income tax purposes. The deferred tax assets and liabilities represent future income tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. The differences relate to the following:

- Depreciable assets' lives and methods of calculating depreciation for financial and income tax reporting.
- Accounting for investments in corporations at fair market value for financial reporting purposes and cost for income tax purposes.

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

NOTE 7 - FEDERAL AND STATE INCOME TAXES (Continued)

The tax effects of temporary differences that give rise to significant portions of deferred tax (assets) liabilities consist of the following:

2009 2008

REDACTED

The provision for (benefits of) income taxes is allocated between operating and nonoperating income as follows:

2009 2008

REDACTED

Components of the provisions for income taxes are as follows:

2009 2008

REDACTED

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

NOTE 8 - LEASES

REDACTED

NOTE 9 - EMPLOYEE BENEFIT PLANS

REDACTED

NOTE 10 - RELATED-PARTY TRANSACTIONS

REDACTED

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NOTES TO FINANCIAL STATEMENTS

December 31, 2009 and 2008

NOTE 10 - RELATED-PARTY TRANSACTIONS (Continued)

2009

2008

REDACTED