

**ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA**

**FINANCIAL STATEMENTS
WITH INDEPENDENT AUDITOR'S REPORT
Years ended June 30, 2012 and 2011**

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

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INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Orange City Communications, L.L.P.
Orange City, Iowa

We have audited the accompanying balance sheets of Orange City Communications, L.L.P. (an Iowa partnership) as of June 30, 2012 and 2011, and the related statements of income, partners' capital 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 audit 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 Orange City Communications, L.L.P. as of June 30, 2012 and 2011, 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 September 17, 2012, on our consideration of Orange City Communications, L.L.P.'s internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. 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 assessing the results of our audit.

Kiesling Associates LLP

Emmetsburg, Iowa
September 17, 2012

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

BALANCE SHEETS
June 30, 2012 and 2011

<u>ASSETS</u>	<u>2012</u>	<u>2011</u>
CURRENT ASSETS		
Cash and cash equivalents	\$ 214,433	\$ 278,678
Accounts receivable:		
Due from customers		
Less allowance of \$848 and \$864, respectively	15,636	19,938
Interexchange carriers		
Less allowance of \$9,518 and \$11,936, respectively	43,959	37,740
Related parties	77,266	256,774
Other	17,224	6,583
Prepayments	1,839	6,342
	<u>370,357</u>	<u>606,055</u>
 PROPERTY, PLANT AND EQUIPMENT		
Telephone plant in service	5,762,819	5,580,391
Video plant in service	39,286	39,286
Internet plant in service	355,919	328,705
	<u>6,158,024</u>	<u>5,948,382</u>
Less accumulated depreciation	2,941,083	2,591,210
	<u>3,216,941</u>	<u>3,357,172</u>
 TOTAL ASSETS	 <u>\$ 3,587,298</u>	 <u>\$ 3,963,227</u>

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

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

BALANCE SHEETS
June 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
<u>LIABILITIES AND PARTNERS' CAPITAL</u>		
CURRENT LIABILITIES		
Current portion of long-term debt	\$ 162,496	\$ 121,092
Accounts payable	48,419	79,521
Customer deposits	300	-
Accrued taxes	108,621	109,937
Accrued interest	2,769	4,827
	<u>322,605</u>	<u>315,377</u>
LONG-TERM DEBT, less current portion	<u>1,311,514</u>	<u>1,486,115</u>
PARTNERS' CAPITAL	<u>1,953,179</u>	<u>2,161,735</u>
TOTAL LIABILITIES AND PARTNERS' CAPITAL	<u>\$ 3,587,298</u>	<u>\$ 3,963,227</u>

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

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

STATEMENTS OF INCOME
Years ended June 30, 2012 and 2011

	2012	2011
OPERATING REVENUES		
Local network services	\$ 670,500	\$ 702,432
Network access services	730,845	597,188
Long distance services	128,597	147,048
Video services	672,872	670,168
Internet services	807,337	728,822
Miscellaneous	20,666	21,581
Service discounts	<u>(255,966)</u>	<u>(260,383)</u>
	<u>2,774,851</u>	<u>2,606,856</u>
 OPERATING EXPENSES		
Plant specific operations	387,350	358,172
Plant nonspecific operations	75,630	39,606
Cost of long distance services	98,484	65,259
Cost of video services	537,534	508,442
Cost of internet services	253,941	235,925
Depreciation	349,873	389,035
Customer operations	124,869	120,557
Corporate operations	207,418	140,496
General taxes	<u>125,046</u>	<u>117,345</u>
	<u>2,160,145</u>	<u>1,974,837</u>
 OPERATING INCOME	 <u>614,706</u>	 <u>632,019</u>
 OTHER INCOME (EXPENSES)		
Interest income	112	284
Interest expense	<u>(73,374)</u>	<u>(121,834)</u>
	<u>(73,262)</u>	<u>(121,550)</u>
 NET INCOME	 <u>\$ 541,444</u>	 <u>\$ 510,469</u>

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

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

STATEMENTS OF PARTNERS' CAPITAL
Years Ended June 30, 2012 and 2011

	<u>Partners' Capital</u>
Balance at June 30, 2010	\$ 2,101,266
Net income	510,469
Distributions	<u>(450,000)</u>
Balance at June 30, 2011	2,161,735
Net income	541,444
Distributions	<u>(750,000)</u>
Balance at June 30, 2012	<u>\$ 1,953,179</u>

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

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

STATEMENTS OF CASH FLOWS
Years ended June 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 541,444	\$ 510,469
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	349,873	389,035
Changes in assets and liabilities:		
(Increase) Decrease in:		
Accounts receivable	166,950	(13,607)
Prepayments	4,503	1,430
Increase (Decrease) in:		
Accounts payable	(31,102)	(95,157)
Accrued taxes	(1,316)	12,831
Other	(1,758)	(80)
Net cash provided by operating activities	<u>1,028,594</u>	<u>804,921</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Capital expenditures	<u>(209,642)</u>	<u>(128,598)</u>
Net cash used in investing activities	<u>(209,642)</u>	<u>(128,598)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment of long-term debt	(133,197)	(108,932)
Distributions to partners	<u>(750,000)</u>	<u>(450,000)</u>
Net cash used in financing activities	<u>(883,197)</u>	<u>(558,932)</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(64,245)	117,391
Cash and Cash Equivalents at Beginning of Year	<u>278,678</u>	<u>161,287</u>
Cash and Cash Equivalents at End of Year	<u>\$ 214,433</u>	<u>\$ 278,678</u>

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

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

NOTES TO FINANCIAL STATEMENTS
June 30, 2012 and 2011

NOTE 1. ORGANIZATION

Orange City Communications, L.L.P. was formed in accordance with Iowa Code Chapter 28E between the City of Orange City, Iowa and Long Lines, L.L.C. and pursuant to the Iowa Uniform Partnership Act. The City of Orange City and Long Lines, L.L.C. participate in the partnership as limited liability partners each with 50% interest. All profits and losses are shared in proportion to ownership interest.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

Orange City Communications, L.L.P. (herein referred to as "the Company") is a provider of local telephone access, long distance telephone services, video services and internet services in Orange City, Iowa.

The accounting policies of the Company conform to accounting principles generally accepted in the United States of America. Management uses estimates and assumptions in preparing its financial statements. Those estimates and assumptions 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 could differ from those estimates. Management has evaluated subsequent events through September 17, 2012, the date the financial statements were available for issue. The accounting records of the telephone company are maintained in accordance with the Uniform System of Accounts for Class A and B Telephone Companies prescribed by the Federal Communications Commission (FCC) as modified by the state regulatory authority.

Cash Equivalents

All highly liquid investments with a maturity of three months or less at the time of purchase are considered cash equivalents.

Accounts Receivable

Accounts receivable are reported net of an allowance for doubtful accounts. The allowance is based on management's estimate of the amount of receivables that will actually be collected. Receivables are considered past due when the amount has been outstanding for thirty days or more.

Property, Plant and Equipment

Property, plant and equipment is capitalized at original cost including the capitalized cost of salaries and wages, materials, certain payroll taxes, and employee benefits.

The Company provides for depreciation for financial reporting purposes on the straight-line method by the application of rates based on the estimated service lives of the various classes of depreciable property. These estimates are subject to change in the near term.

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

NOTES TO FINANCIAL STATEMENTS
June 30, 2012 and 2011

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property, Plant and Equipment (Continued)

Renewals and betterments of units of telephone property are charged to telephone plant in service. When telephone plant is retired, its cost is removed from the asset account and charged against accumulated depreciation less any salvage realized. No gains or losses are recognized in connection with routine retirements of depreciable telephone property. Repairs and renewals of minor items of telephone property are included in plant specific operations expense.

Repairs of video and internet property, as well as renewals of minor items, are charged to plant specific operations expense. A gain or loss is recognized when video and internet property is sold or retired.

Asset Retirement Obligations

Generally accepted accounting principles require entities to record the fair value of a liability for legal obligations associated with an asset retirement in the period in which the obligations are incurred. When the liability is initially recorded, the entity capitalizes the cost of the asset retirement obligation by increasing the carrying amount of the related long-lived asset. Over time, the liability is accreted to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset.

The Company has determined it does not have a material legal obligation to remove long-lived assets, and accordingly, there have been no liabilities recorded for the years ended June 30, 2012 and 2011.

Long-Lived Assets

The Company would provide for impairment losses on long-lived assets when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying amount. Based on current conditions, management does not believe any of its long-lived assets are impaired.

Income Taxes

Under provisions of the Internal Revenue Code, the partners include their respective shares of Company income or loss on their individual tax returns. Accordingly, no provision for income taxes has been made in the accompanying financial statements. The Company's federal and state tax returns for years 2008 to present remain subject to examination.

Revenue Recognition

The Company recognizes revenues when earned regardless of the period in which they are billed.

Local network service, video and internet revenues are recognized over the period a subscriber is connected to the network.

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

NOTES TO FINANCIAL STATEMENTS
June 30, 2012 and 2011

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition (Continued)

Network access and long distance service revenues are derived from charges for access to the Company's local exchange network. The interstate and intrastate access revenues are based upon the Company's tariffs for access charges filed with the relevant regulatory agencies. Network access and long distance revenues are recognized at the time a call is placed based on the minutes of traffic processed at tariffed or contracted rates.

The Company recognizes taxes charged to customers on a net basis in the statements of income.

Fair Value Measurements

The Company determined the fair value of its financial assets and liabilities based on the fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following three levels of inputs may be used to measure fair value:

- Level 1 Quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.
- Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Reclassifications

Certain reclassifications have been made to the 2011 financial statements to conform with the 2012 presentation.

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

NOTES TO FINANCIAL STATEMENTS
June 30, 2012 and 2011

NOTE 3. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment includes the following:

	2012	2011
Telephone plant in service:		
Buildings	\$ 8,839	\$ 8,839
Furniture and office equipment	38,403	37,684
Vehicles and work equipment	116,514	111,106
Central office assets	472,976	472,976
Cable and wire facilities	4,945,002	4,788,149
Other plant and equipment	181,085	161,637
Subtotal	5,762,819	5,580,391
Video plant in service:		
Head end equipment	39,286	39,286
Internet plant in service:		
Internet equipment	355,919	328,705
Total property, plant and equipment	\$ 6,158,024	\$ 5,948,382

Depreciation on depreciable property resulted in composite rates of 5.78% and 6.60% for 2012 and 2011, respectively.

NOTE 4. LONG-TERM DEBT

Long-term debt consists of:

	2012	2011
Northwestern State Bank of Orange City - 4.25%	\$ 1,474,010	\$ 1,607,207
Less current portion	162,496	121,092
	\$ 1,311,514	\$ 1,486,115

The annual requirements for principal payments on long-term debt for the next five years are as follows:

2013	\$	162,496
2014		169,538
2015		176,885
2016		184,551
2017		192,549

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

NOTES TO FINANCIAL STATEMENTS
June 30, 2012 and 2011

NOTE 4. LONG-TERM DEBT (Continued)

Substantially all assets of the Company are pledged as security for the long-term debt under certain loan agreements with the Northwestern State Bank of Orange City. These mortgage notes are to be repaid in equal monthly installments covering principal and interest beginning after date of issue and expiring by 2020.

Cash paid for interest, net of amounts capitalized for 2012 and 2011, totaled \$75,432 and \$121,564, respectively.

At June 30, 2012, of the funds available for long-term notes and lines of credit, all funds were advanced.

NOTE 5. LEASES

The Company is leasing various facilities and equipment on a monthly basis under an operating lease agreement. Total lease expense was \$48,000 for the years ended June 30, 2012 and 2011. The entire expense for the year ended June 30, 2012 and 2011 was paid to a related party.

NOTE 6. RELATED PARTY TRANSACTIONS

The Company regularly conducts business with a variety of entities related through common ownership. The following is a summary of transactions and balances with related parties as of June 30, 2012 and 2011 and for the years then ended:

	<u>2012</u>	<u>2011</u>
Plant specific operations	\$ <u>465,228</u>	\$ <u>396,124</u>
Cost of internet services	\$ <u>253,941</u>	\$ <u>235,925</u>
Customer operations	\$ <u>92,263</u>	\$ <u>95,615</u>
Corporate operations	\$ <u>90,000</u>	\$ <u>90,000</u>
Property and equipment expenditures	\$ <u>23,391</u>	\$ <u>5,791</u>
Accounts receivable	\$ <u>77,266</u>	\$ <u>256,774</u>

ORANGE CITY COMMUNICATIONS, L.L.P.
ORANGE CITY, IOWA

NOTES TO FINANCIAL STATEMENTS
June 30, 2012 and 2011

NOTE 7. RELATED PARTY COMMITMENTS

The Company has a maintenance agreement with Long Lines, L.L.C. The Company has agreed to pay Long Lines, L.L.C. \$7,500 per month to operate the utility plant and provide management and accounting services. The agreement specified an initial term of five years, expiring July 31, 2008, and automatically renews for twelve month periods, unless either party provides written notice prior to expiration.

The Company has entered into a long-term agreement with Pioneer Internet (an affiliate of Long Lines, L.L.C.) for the provision of wholesale internet services. Services agreed to include access to wholesale internet service and the related transport and connectivity. The expenses for services provided under the agreement were \$253,941 and \$235,925 in 2012 and 2011, respectively. The agreement specified an initial term of sixty months, beginning in 2001, and is automatically renewable for additional twelve month periods, unless either party provides written notice prior to expiration.

NOTE 8. CONCENTRATIONS OF CREDIT RISK

The Company grants credit to local service customers, all of whom are located in the franchised service area, and telecommunications intrastate and interstate long distance carriers.

The Company is subject to competition for telecommunications services including telecommunications exchange services offered by other providers in the service area.

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash and cash equivalents.

The Company maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant credit risk on cash and cash equivalents.



**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT
OF THE FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

To the Board of Directors
Orange City Communications, L.L.P.
Orange City, Iowa

We have audited the accompanying financial statements of Orange City Communications, L.L.P. as of and for the year ended June 30, 2012, and have issued our report thereon dated September 17, 2012. We conducted our audit 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Orange City Communications, L.L.P.'s internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Company's internal control over financial reporting.

Our consideration of the internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. In addition, because of inherent limitations in internal control, including the possibility of management override of controls, misstatements due to error or fraud may occur and not be detected by such controls.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented or detected and corrected on a timely basis. We did not identify any deficiencies in internal control that we consider to be material weaknesses.

A significant deficiency is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Orange City Communications, L.L.P.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

This report is intended solely for the information and use of the board of directors, management of the Company, and federal and state regulatory agencies and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Kiesling Associates LLP

Emmetsburg, Iowa
September 17, 2012