FINGER LAKES REGIONAL TELECOMMUNICATIONS DEVELOPMENT CORP.

CANANDAIGUA, NEW YORK

AUDITED FINANCIAL STATEMENTS

AND

INDEPENDENT AUDITORS' REPORT

DECEMBER 31, 2009 AND 2008

CONTENTS

MMB
MENGEL METZGER BARR & CO. LLP
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

Board of Directors
Finger Lakes Regional Telecommunications Development Corp.

We have audited the accompanying statements of financial position of Finger Lakes Regional Telecommunications Development Corp. as of December 31, 2009 and 2008, and the related statements of activities and changes in net assets (deficit) and cash flows for the years then ended. These financial statements are the responsibility of the Organization'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. 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Organization's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 Finger Lakes Regional Telecommunications Development Corp. as of December 31, 2009 and 2008, and the changes in its net assets (deficit) and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Mengel, Metzger, Barr & Co. LLP

Rochester, New York
February 22, 2010

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FINGER LAKES REGIONAL TELECOMMUNICATIONS DEVELOPMENT CORP.

STATEMENTS OF FINANCIAL POSITION

	December 31, 2009	December 31, 2008
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 119,130	$ 1,043,383
Accounts receivable	20,092	-
Prepaid expenses	4,876	2,146
TOTAL CURRENT ASSETS	144,098	1,045,529
PROPERTY AND EQUIPMENT, net of accumulated depreciation of $35,331 at December 31, 2009	2,317,424	1,240,222
OTHER ASSETS		
Loan acquisition costs	145,882	-
Restricted cash	377,859	-
	523,741	-
	$ 2,985,263	$ 2,285,751
LIABILITIES AND UNRESTRICTED NET ASSETS (DEFICIT)		
CURRENT LIABILITIES		
Accounts payable - trade	$ 192,188	$ 36,500
Current portion of deferred revenue	45,652	40,000
TOTAL CURRENT LIABILITIES	237,840	76,500
OTHER LIABILITIES		
Deferred revenue	1,023,764	930,000
Long-term debt	1,715,898	1,500,000
	2,739,662	2,430,000
UNRESTRICTED NET ASSETS (DEFICIT)	7,761	(220,749)
	$ 2,985,263	$ 2,285,751

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

FINGER LAKES REGIONAL TELECOMMUNICATIONS DEVELOPMENT CORP.

STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS (DEFICIT)

	Year ended December 31, 2009	Year ended December 31, 2008
Revenue	$ 130,782	$ 30,000
Costs and expenses:		
Marketing and sales	113,023	62,990
Education and training	-	198
Insurance	8,331	8,714
Legal and accounting	41,670	46,400
Network operations	68,768	1,911
Office expense	17,249	1,468
Depreciation	35,331	-
	284,372	121,681
LOSS FROM OPERATIONS	(153,590)	(91,681)
Other income:		
Interest income	2,863	49,236
Empire Pipeline revenue	379,237	-
	382,100	49,236
INCREASE (DECREASE) IN NET ASSETS	228,510	(42,445)
Unrestricted net assets (deficit) at beginning of year	(220,749)	(178,304)
UNRESTRICTED NET ASSETS (DEFICIT) AT END OF YEAR	$ 7,761	$ (220,749)

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

FINGER LAKES REGIONAL TELECOMMUNICATIONS DEVELOPMENT CORP.

STATEMENTS OF CASH FLOWS

	Year ended December 31, 2009	2008
CASH FLOWS - OPERATING ACTIVITIES		
Change in net assets	$ 228,510	$ (42,445)
Adjustments to reconcile change in net assets to net cash provided from (used for) operating activities:		
Depreciation	35,331	-
Changes in certain assets and liabilities affecting operations:		
Accounts receivable	(20,092)	-
Prepaid expenses	(2,730)	36
Trade accounts payable	(18,688)	22,926
Deferred revenue	99,416	(30,000)
NET CASH PROVIDED FROM (USED FOR) OPERATING ACTIVITIES	321,747	(49,483)
CASH FLOWS - INVESTING ACTIVITIES		
Decrease in security deposits	-	3,000
Purchase of property and equipment	(938,157)	(1,124,931)
NET CASH USED FOR INVESTING ACTIVITIES	(938,157)	(1,121,931)
CASH FLOWS - FINANCING ACTIVITIES		
Increase in loan acquisition costs	(145,882)	-
Proceeds from long-term debt	215,898	-
Increase in restricted cash	(377,859)	-
NET CASH USED FOR FINANCING ACTIVITIES	(307,843)	-
NET DECREASE IN CASH AND CASH EQUIVALENTS	(924,253)	(1,171,414)
Cash and cash equivalents at beginning of year	1,043,383	2,214,797
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 119,130	$ 1,043,383
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid during the year for interest and capitalized	$ 1,361	$ -
NON-CASH OPERATING AND INVESTING ACTIVITY		
Capitalized property and equipment included in accounts payable	$ 174,376	$ -

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

NOTE A: THE ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Organization
Finger Lakes Regional Telecommunications Development Corp. (the “Organization”) is a not-for-profit corporation that was formed to develop, operate, market and manage a municipal-based open access fiber optic backbone in Ontario County. The Organization is managed by a local board of directors.

Basis of accounting
The accompanying financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America.

Financial statement presentation
The Organization is required to report information regarding its financial position and activities according to three classes of net assets: unrestricted net assets, temporarily restricted net assets, and permanently restricted net assets.

Unrestricted Net Assets: Represents all resources over which the Governing Board has discretionary control to use in carrying on the Organization’s operations in accordance with the guidelines established for the Organization. The Board may designate portions of the current unrestricted net assets for specific purposes, projects or investment.

Temporarily Restricted Net Assets: Consists of all resources currently available for use, but limited by donor imposed restrictions that expire by the passage of time or can be fulfilled or otherwise removed by actions of the Organization. The Organization had no temporarily restricted net assets at December 31, 2009 and 2008.

Permanently Restricted Net Assets: Represents the principal amount of gifts and bequests accepted with the donor-stipulation that the principal be maintained intact in perpetuity and that only the investment income earned may be expended for general purposes. The Organization had no permanently restricted net assets at December 31, 2009 and 2008.

Cash and cash equivalents
The Organization maintains cash balances at financial institutions located in upstate New York. Cash and certain money market account balances are insured by the Federal Deposit Insurance Corporation up to $250,000 at each institution. In addition, in accordance with the Federal Deposit Insurance Corporation’s Temporary Liquidity Program, certain non-interest bearing transaction accounts at the financial institutions were 100% insured through December 31, 2009. There were no uninsured balances December 31, 2009. The Organization has not experienced any losses in such accounts and management believes it is not exposed to any significant risk in cash or cash equivalents.

Accounts receivable
Accounts receivable are stated at the amount billed to customers for leases of dark fiber or other charges incurred. Management reviews accounts receivable on a periodic basis to determine if any receivables will potentially be uncollectible. Based on the information available, the Organization believes no allowance for doubtful accounts was necessary as of December 31, 2009.

NOTE A: THE ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Cont'd

Property and equipment

Property and equipment consists primarily of costs to construct the fiber optic network and are recorded at cost. Depreciation is computed using the straight-line method on a basis considered adequate to depreciate the assets over their estimated useful lives, which are generally twenty-five years.

Expenditures for renewals and betterments are capitalized while expenditures for repairs and maintenance are charged to activities as incurred. Upon sale or retirement, the related cost and accumulated depreciation are removed from the accounts and any related gain or loss is reflected in the statement of activities.

The Organization capitalizes interest costs incurred on funds used to construct fixed assets. The capitalized interest is recorded as part of the assets to which it related and is amortized over the asset's estimated useful life. Interest cost capitalized during the year ended December 31, 2009 was $1,361.

Loan acquisition costs

Loan acquisition costs are stated at cost and will be amortized over the term of the loan agreement, which is 24 years, beginning at the time the loan is converted to a term loan as described in Note E.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at December 31, 2009 and 2008 and the reported amounts of revenue and expenses for the years then ended. Actual results could differ from those estimates.

Tax exempt status

The Organization is tax-exempt under section 501(c)(3) of the Internal Revenue Code. The Organization has filed for and received an income tax exemption in New York State. The Organization files Form 990 tax returns in the U.S. federal jurisdiction and in New York State. With few exceptions, the Organization is no longer subject to U.S. federal or state income tax examinations by tax authorities for years before 2006. Years 2006, 2007, 2008 and 2009 are still subject to potential audit by the IRS and the taxing authorities in New York State. The Organization adopted the provisions of FASB ASC 740-10 *Accounting for Uncertainty in Income Taxes* (formerly FIN 48), and its related amendment on January 1, 2009. Management of the Organization believes it has no material uncertain tax positions and, accordingly it has not recognized any liability for unrecognized tax benefits.

Subsequent events

The Organization as conducted an evaluation of potential subsequent events occurring after the statement of financial position date through February 22, 2010, which is the date the financial statements are available to be issued. No subsequent events requiring disclosure were noted.

Reclassifications

Certain 2008 amounts have been reclassified to conform with the 2009 presentation.

NOTE B: OPERATIONS

The fiber optic backbone is available or open to any entity within Ontario County and parts of Wayne County that wish to use it. The Organization contracts with the private sector for operating and administrative services.

The Organization generates a significant portion of its ongoing revenue by leasing space on the fiber optic backbone to two different customer types. These customer types are described below:

Carrier – These customers will include nationally and regionally-known wireless providers and internet service providers.

Enterprise – These customers will typically consist of hospitals, school districts, colleges and private businesses.

NOTE C: PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	December 31,	
	2009	2008
Fiber Network - Phase I	$ 1,162,914	$ -
Fiber Network - Phase II	250,169	-
Fiber Network - Wayne Finger Lakes BOCES	140,403	-
Fiber Network - Fishers Laterals	73,106	-
Construction-in-progress	726,163	1,240,222
	2,352,755	1,240,222
Less accumulated depreciation	35,331	-
	$ 2,317,424	$ 1,240,222

The Organization began developing the fiber optic backbone in October 2007. Construction in progress represents the costs incurred before the respective segments of the fiber optic backbone are placed into service. At December 31, 2009 and 2008, the construction in progress was $726,163 and $1,240,222, respectively. The entire fiber optic backbone is expected to be approximately 180 miles in total length and is expected to cost approximately $5,800,000.

NOTE D: RESTRICTED CASH

Restricted cash consists of unexpended funds which are restricted for the future payments of principal and interest due on the construction and lateral loans. (See Note E). Amounts are held at a financial institution and are insured up to $250,000 by the Federal Deposit Insurance Corporation as of December 31, 2009.

NOTE E: LONG-TERM DEBT

Long-term debt of the Organization is as follows:

	December 31, 2009	December 31, 2008
On September 15, 2006, the Organization entered into an agreement with the County of Ontario (the "County") whereby the County extended to the Organization a one-time interest-free loan in the amount of $1,500,000. The loan will be repaid to the County upon retirement of the Organization's bank debt, or the termination date of the agreement (Year 2033), whichever occurs earlier. This loan is subordinated to the bank debt described below.	$ 1,500,000	$ 1,500,000
Under a 2009 agreement with a bank, the Organization has a non-replenishing line of credit arrangement (the "Construction Line") with maximum borrowings of $4,393,331 and interest charged at a a variable rate based on LIBOR plus 2.5% (effective rate of 2.7329% at December 31, 2009). Under the same agreement, the Organization has another non-replenishing line of credit arrangement (the "Lateral Line of Credit") with maximum borrowings of $1,200,000 and interest charged at a variable rate based on LIBOR plus 2.5% (effective rate of 2.7329% at December 31, 2009). The Organization may request advances on these lines until December 31, 2010, at which point the balance will convert to a term loan. Repayments of the term loan will be based on a 24 year amortization schedule with a balloon payment of the remaining balance due after 5 years. At December 31, 2009, $215,898 is outstanding against the Construction Line of Credit. There were no borrowings on the Lateral Line of Credit at December 31, 2009. These lines are secured by substantially all assets of the Organization and the revenues provided by the Host Community Agreement (see Note H for further details). Under the terms of this agreement, the Organization is required among other things, to meet certain financial covenants. As of December 31, 2009 the Organization is in compliance with these covenants. On April 30, 2009, with an effective date of December 31, 2010 and a maturity of September 2034, the Organization entered into an interest rate swap contract to hedge its exposure to changes in the variable rate loan agreement. In accordance with that agreement, the interest on the "Construction Line of Credit" will be swapped to a fixed rate of 4.5% with the Organization receiving LIBOR, this results in an effective rate of 7%. The Organization anticipates entering a separate interest rate swap contract at the time borrowings are made under the "Lateral Line of Credit". The value of this swap contract at December 31, 2009 has not been recorded as it is not material to the financial statements.	215,898	-
	$ 1,715,898	$ 1,500,000

NOTE E: LONG-TERM DEBT, Cont'd

Repayments of the above agreements are expected to be as follows:

Year ending December 31	Amount
2010	$ -
2011	8,996
2012	8,996
2013	8,996
2014	8,996
Thereafter	1,679,914
	$ 1,715,898

NOTE F: DEFERRED REVENUE

The County paid to the Organization a one-time prepayment for all services rendered pursuant to the agreement in the amount of $500,000 as well as an additional $500,000 one-time prepayment for connecting all buildings in the Hopewell Complex to a single point where it will then be connected to the rest of the ring pursuant to the agreement. These amounts have been recorded as deferred revenue and are being recognized as earned revenue as the services are performed in accordance with the terms of the agreement beginning April 2008. At December 31, 2009 and 2008, deferred revenue related to this agreement was $930,000 and $970,000, respectively. The deferred revenue will be amortized over the term of the contract at a rate of $40,000 per year over twenty-five years. The contract with the County is at a below market rate, which is not ascertainable at this time.

In addition, during 2009, the Organization received an up-front payment from a customer to provide a connection to the fiber ring as well as maintenance revenue for a 25 year period. The deferred revenue will be amortized over the term of the contract at a rate of $5,652 per year over twenty-five years. At December 31, 2009, deferred revenue relating to this agreement was $139,416.

NOTE G: TRANSACTIONS WITH THE COUNTY OF ONTARIO

The County, in consideration for the above-referenced services and to cover monthly maintenance costs, will allow the Organization to use County meeting rooms, use the County Web server to host the initial Organization website, the services of the Chief Information Officer to serve as the Chief Executive Officer of the Organization and the services of other County employees or officers to serve on the Organization's Board of Directors or perform other duties as authorized by the County's Board of Supervisors. No amounts have been recorded for the County's contributed services during the years ended December 31, 2009 and 2008 which would be offset by the applicable expense.

The County has also provided financing as described in Note E and an up-front payment for services to be provided as described in Note F.

NOTE H: COMMITMENTS

Empire Pipeline, Inc.

A portion of the Organization's revenues are derived from payments made by Empire State Pipeline (a joint venture) and Empire Pipeline, Inc. (collectively "Empire") as a result of a Host Community Benefit Agreement (the "Agreement") entered into between Empire and the Organization on July 1, 2007. The agreement is related to a separate payment-in-lieu-of-tax ("PILOT") agreement entered into between Empire and the Ontario County Industrial Development Agency. The Agreement stipulates that Empire pay the Organization $379,237 annually for twenty-five years. Payments of $94,809 are due quarterly. The payments are guaranteed by National Fuel Gas Company, a publicly-traded corporation and parent organization of Empire. These payments provide a guaranteed revenue stream to the Organization, and are recognized as revenue when the payments become due and payable. Revenues from this agreement totaled $379,237 for the year ended December 31, 2009. There were no revenues from this agreement for the year ended December 31, 2008. Funds received under this agreement are assigned to the bank, as described in Note E, as security for the "Construction Line of Credit" and "Lateral Line of Credit".

NOTE I: MINIMUM RENTALS

The Company is the lessor of fiber optic cable under operating leases expiring in various years through 2034. For the year ended December 31, 2009, two customers accounted for approximately 52% of total operating revenue. For the year ended December 31, 2008, one customer accounted for 100% of total operating revenue.

Future minimum rents receivable under non-cancelable operating leases are approximately as follows:

Year ending December 31	Amount
2010	$ 240,000
2011	322,200
2012	322,200
2013	322,200
2014	298,000