

**UPSTATE TELECOMMUNICATIONS CORPORATION**

**Financial Statements as of  
December 31, 2010 and 2009  
Together with  
Independent Auditors' Report**

**Bonadio & Co., LLP**  
Certified Public Accountants

## INDEPENDENT AUDITORS' REPORT

March 21, 2011

To the Board of Directors of  
Upstate Telecommunications Corporation:

We have audited the accompanying balance sheets of Upstate Telecommunications Corporation (a New York not-for-profit corporation) (UTC) as of December 31, 2010 and 2009, and the related statements of activities and change in net assets and cash flows for the years then ended. These financial statements are the responsibility of UTC'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 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 UTC as of December 31, 2010 and 2009, and the changes in its net assets and its cash flows for the for the years then ended, in conformity with accounting principles generally accepted in the United States.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 21, 2011 on our consideration of UTC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and 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 considered in assessing the results of our audit.

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# UPSTATE TELECOMMUNICATIONS CORPORATION

## BALANCE SHEETS

DECEMBER 31, 2010 AND 2009

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	<u>2010</u>	<u>2009</u>
<b>ASSETS</b>		
CURRENT ASSETS:		
Cash	\$ 1,502,371	\$ 1,240,368
Prepaid expenses and other current assets	246,247	100,828
Current portion of investment in direct-financing lease	<u>573,727</u>	<u>560,067</u>
Total current assets	<u>2,322,345</u>	<u>1,901,263</u>
NONCURRENT ASSETS:		
Fixed assets, net	1,145,842	1,397,763
Investment in direct-financing lease, net of current portion	6,117,021	6,690,748
Debt issuance costs, net	558,431	619,397
Limited use assets	<u>6,733,680</u>	<u>6,089,075</u>
Total noncurrent assets	<u>14,554,974</u>	<u>14,796,983</u>
Total assets	<u>\$ 16,877,319</u>	<u>\$ 16,698,246</u>
<b>LIABILITIES AND NET ASSETS</b>		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	\$ 172,149	\$ 200,053
Current portion of capital lease obligation	251,241	240,009
Current portion of bonds payable	<u>2,100,000</u>	<u>2,050,000</u>
Total current liabilities	2,523,390	2,490,062
INTEREST RATE SWAP LIABILITY	1,900,669	1,626,637
CAPITAL LEASE OBLIGATION, net of current portion	1,859,584	2,110,825
BONDS PAYABLE, net of current portion	<u>22,390,000</u>	<u>24,490,000</u>
Total liabilities	28,673,643	30,717,524
NET ASSETS	<u>(11,796,324)</u>	<u>(14,019,278)</u>
Total liabilities and net assets	<u>\$ 16,877,319</u>	<u>\$ 16,698,246</u>

The accompanying notes are an integral part of these statements.

# UPSTATE TELECOMMUNICATIONS CORPORATION

## STATEMENTS OF ACTIVITIES AND CHANGE IN NET ASSETS FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009

	<u>2010</u>	<u>2009</u>
REVENUES:		
Maintenance and support services	\$ 6,418,370	\$ 6,438,925
Leasing revenue	925,017	924,928
Interest on investment in direct-financing lease	254,248	275,531
Investment loss, net	(3,821)	(3,986)
Other	12,959	-
	<u>7,606,773</u>	<u>7,635,398</u>
Total revenues		
EXPENSES:		
Project costs -		
Hosting, training, and implementation	1,575,617	1,161,551
Interest, amortization and fees	1,454,866	1,446,663
Network management and maintenance	824,041	706,044
Management services	445,216	443,486
Copier maintenance	263,555	244,086
Amortization	260,932	259,568
Other	118,232	104,811
	<u>4,942,459</u>	<u>4,366,209</u>
Total project costs		
Administration -		
Professional fees	166,548	117,333
Other	780	280
	<u>167,328</u>	<u>117,613</u>
Total administration		
Total expenses	<u>5,109,787</u>	<u>4,483,822</u>
CHANGE IN NET ASSETS FROM OPERATIONS	2,496,986	3,151,576
OTHER:		
Gain (loss) on interest rate swap agreement	<u>(274,032)</u>	<u>621,173</u>
CHANGE IN NET ASSETS	2,222,954	3,772,749
NET ASSETS - beginning of year	<u>(14,019,278)</u>	<u>(17,792,027)</u>
NET ASSETS - end of year	<u>\$ (11,796,324)</u>	<u>\$ (14,019,278)</u>

The accompanying notes are an integral part of these statements.

# UPSTATE TELECOMMUNICATIONS CORPORATION

## STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009

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	<u>2010</u>	<u>2009</u>
CASH FLOW FROM OPERATING ACTIVITIES:		
Change in net assets	\$ 2,222,954	\$ 3,772,749
Adjustments to reconcile change in net assets to net cash flow from operating activities:		
Amortization expense	260,932	259,568
Amortization of debt issuance costs	60,966	60,966
(Gain) loss on interest rate swap agreement	274,032	(621,173)
Changes in:		
Prepaid expenses and other current assets	(145,419)	15,173
Change in accounts payable and accrued expenses	<u>(27,904)</u>	<u>45,769</u>
Net cash flow from operating activities	<u>2,645,561</u>	<u>3,533,052</u>
CASH FLOW FROM INVESTING ACTIVITIES:		
Payments under direct-financing lease	560,067	546,406
Purchases of fixed assets	(9,011)	(12,463)
Purchases of limited use assets	(18,627,056)	(10,639,387)
Proceeds from sale of limited use assets	<u>17,982,451</u>	<u>9,027,537</u>
Net cash flow from investing activities	<u>(93,549)</u>	<u>(1,077,907)</u>
CASH FLOW FROM FINANCING ACTIVITIES:		
Repayment on capital lease obligation	(240,009)	(229,279)
Repayment on bonds payable	<u>(2,050,000)</u>	<u>(2,000,000)</u>
Net cash flow from financing activities	<u>(2,290,009)</u>	<u>(2,229,279)</u>
CHANGE IN CASH	262,003	225,866
CASH - beginning of year	<u>1,240,368</u>	<u>1,014,502</u>
CASH - end of year	<u>\$ 1,502,371</u>	<u>\$ 1,240,368</u>

The accompanying notes are an integral part of these statements.

# UPSTATE TELECOMMUNICATIONS CORPORATION

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2010 AND 2009

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### 1. THE ORGANIZATION

Upstate Telecommunications Corporation (UTC) is a New York not-for-profit corporation organized in March 2005 to provide technology and telecommunications services to Monroe County (the County). UTC was formed as a local development corporation of the County. All service revenue derived by UTC is currently received solely from the County and as such UTC's existence is dependent upon this continuing relationship. Although the County is not financially accountable for UTC, it does appoint a voting majority of the board and as such is considered a related party to UTC.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### **Basis of Accounting**

UTC's financial statements have been prepared in conformity with accounting principles generally accepted in the United States.

#### **Financial Reporting**

All of UTC's net assets were unrestricted at December 31, 2010 and 2009.

#### **Cash**

Cash consists of bank demand deposit accounts. At times, the balances in these accounts may exceed federally insured limits. UTC has not experienced any losses in these accounts and believes it is not exposed to any significant credit risk with respect to cash.

#### **Fixed Assets**

Fixed assets are recorded at cost, if purchased, or fair value at the date of donation. UTC capitalizes equipment purchases with a cost greater than \$1,000, which have useful lives greater than one year. Fixed assets consist of photocopying equipment used by its primary customer. Amortization is provided using the straight-line method over the assets' estimated useful lives, or seven (7) years, or the lease term which ever is shorter.

#### **Investment in Direct-Financing Lease**

The cost of telecommunications equipment purchased by UTC and leased to the County is recorded as a direct-financing lease. Unearned income is calculated using the interest rate in place on the bonds that were issued to facilitate the purchase of the underlying equipment. Lease principal payments are recognized concurrent with the repayment schedule on the outstanding bonds.

#### **Debt Issuance Costs**

Costs incurred in connection with bond and debt issuances have been capitalized and are being amortized on the straight-line method over the 15-year term of the bonds or the 12-year term of the capital lease obligation, respectively.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### Limited Use Assets

Limited use assets consist of funds required by the bond agreement and are invested in money market funds or U.S. government obligations and are recorded at fair market value based on quoted market prices. Interest, dividends and gains (losses) on limited use assets are shown as investment income (loss), net in the accompanying financial statements.

### Fair Value Measurement - Definition and Hierarchy

Accounting Standards Codification (ASC) 820, *Fair Value Measurements*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

UTC uses various valuation techniques in determining fair value. ASC 820 establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of UTC. Unobservable inputs are inputs that reflect UTC's assumptions about the assumptions market participants would use in pricing the liability, developed based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

- Level 1 - Valuations based on quoted prices in active markets for identical assets or liabilities that UTC has the ability to access. Valuation adjustments are not applied to Level 1 instruments. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these products does not entail a significant degree of judgment.

UTC's U.S. government money market funds utilize Level 1 inputs.

- Level 2 - Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, directly or indirectly.

UTC's mortgage-backed securities utilize Level 2 inputs.

- Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement.

UTC's interest rate swap contract is valued utilizing Level 3 inputs.

The availability of observable inputs can vary and is affected by a wide variety of factors. To the extent that a valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised by UTC in determining fair value is greatest for instruments categorized in Level 3. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, for disclosure purposes the level in the fair value hierarchy within which the fair value measurement in its entirety falls is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

### **Fair Value Measurement - Definition and Hierarchy (Continued)**

Fair value of UTC's interest rate swap contract is derived using the difference between the average value of the SIFMA Index over all possible future interest rate environments, discounted to the present time as calculated by the bank and the fixed rate interest at the stated rate in the swap agreement.

Fair value of UTC's mortgage-backed securities is valued at the quoted price of the underlying assets of the pool.

### **Financial Interests Measured at Fair Value**

UTC has financial instruments which are recorded at fair value in the accompanying balance sheets. UTC made estimates regarding the valuation of the liability associated with the interest rate swap contract measured at fair value in the financial statements.

The fair values of long-term debt are based on quoted market prices for the same or similar issues or on the current rates offered to UTC for debt of the same remaining maturities.

### **Income Taxes**

UTC is a not-for-profit corporation organized pursuant to sections 402 and 1411 of the New York State Not-for-Profit Corporation law and is, therefore, exempt from income taxes. UTC is also exempt from Federal reporting requirements under Internal Revenue Service Revenue Procedure 95-48, 1995-2 C.B. 418 as a governmental unit or affiliate of a governmental unit described in the procedure.

For tax exempt entities, their tax-exempt status itself is deemed to be an uncertainty, since events could potentially occur to jeopardize their tax-exempt status. As of December 31, 2010 and 2009, UTC does not have a liability for unrecognized tax benefits, nor does it file federal or New York State income tax returns.

### **Revenue Recognition**

- Interest on investment in direct-financing lease - The interest imputed over the term of the direct-financing lease is recorded in this financial category.
- Maintenance and Support Services - Under UTC's agreement with the County, annual payments received are also intended to cover operating costs incurred in connection with the agreement such as maintenance of equipment, technology upgrades, license fees, and technology support. The portion of the County's annual payment not allocated to interest or payment of principal is recorded as maintenance and support revenue.
- Leasing Revenue - Leasing revenue is recognized in accordance with the operating lease agreement with the County (See Note 11). Amounts recorded are intended to cover UTC's costs for maintenance, insurance, management fees, and other costs associated with servicing the installed equipment.

### **Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

### **Reclassifications**

Certain prior year amounts have been reclassified to conform with the current year presentation.

### 3. FIXED ASSETS

Fixed assets consisted of the following at December 31:

	<u>2010</u>	<u>2009</u>
Assets under capital lease:		
Copier equipment	\$ 1,831,029	\$ 1,822,018
Less: Accumulated amortization	<u>(685,187)</u>	<u>(424,255)</u>
	<u>\$ 1,145,842</u>	<u>\$ 1,397,763</u>

### 4. INVESTMENT IN DIRECT-FINANCING LEASE

UTC has leased its telecommunications equipment to Monroe County under the terms of a direct-financing lease agreement that states that UTC will be paid average annual payments of approximately \$6,200,000 per year by Monroe County commencing February 7, 2005 and terminating February 2, 2021. The annual lease payments also cover certain operating costs such as maintenance, technology upgrades and license fees. The annual continuation of this agreement is solely dependent upon appropriations granted by Monroe County under the annual budgetary process and therefore is not guaranteed. The portion of the annual lease payments relating to the operating costs and future equipment upgrades have not been included in the investment in direct-financing lease on the accompanying balance sheet. The following table summarizes the components of the direct-financing lease at December 31:

	<u>2010</u>	<u>2009</u>
Future lease payments - gross	\$ 7,890,978	\$ 8,705,294
Less: Unearned income (3.8% interest)	<u>(1,200,230)</u>	<u>(1,454,479)</u>
	<u>\$ 6,690,748</u>	<u>\$ 7,250,815</u>

Future scheduled payments under this agreement are as follows for the years ending December 31:

2011	\$ 573,727
2012	601,047
2013	611,975
2014	640,662
2015	670,714
Thereafter	<u>3,592,623</u>
	<u>\$ 6,690,748</u>

#### Revenue Concentration

The revenue that UTC recognized during 2010 and 2009 is composed almost exclusively of the long-term and operating leases of its equipment to Monroe County.

### 5. DEBT ISSUANCE COSTS

The debt issuance costs capitalized as of December 31, 2010 and 2009 were \$906,982, and amortization expense for each of the years 2010 and 2009 was \$60,966. Accumulated amortization at December 31, 2010 and 2009 was \$348,551 and \$287,585, respectively.

## 6. LIMITED USE ASSETS

Limited use assets consist of investments held by UTC as follows at December 31:

	<u>2010</u>	<u>2009</u>
U.S. Government money market funds	\$ 6,153,732	\$ 6,089,075
Mortgage-backed securities	<u>579,948</u>	<u>-</u>
	<u>\$ 6,733,680</u>	<u>\$ 6,089,075</u>

At December 31, 2010 and 2009, \$2,358,174 and \$2,433,309, respectively, of the investments are designated for debt service payments. The remaining investments are designated for funding future capital or operating costs of UTC.

Net investment income (loss) consisted of the following for the years ended December 31:

	<u>2010</u>	<u>2009</u>
Interest and dividend income	\$ 6,088	\$ 11,727
Investment management fees	<u>(9,909)</u>	<u>(15,713)</u>
	<u>\$ (3,821)</u>	<u>\$ (3,986)</u>

## 7. BONDS PAYABLE

UTC issued Series 2005 Variable Rate Demand Information Technology Revenue Bonds (the Bonds) in order to fund a telecommunications and technology project. The Bonds were issued on March 30, 2005 in the amount of \$32,465,000 and mature on March 1, 2020. The bondholders are paid interest monthly on the bonds at a variable rate (0.3% at December 31, 2010) as determined by the bank semi-annually on January 1 and July 1 of each year. The Bonds are subject to redemption, prior to maturity, at the option of the bank. The Bonds are collateralized under the terms of the bond agreement. The collateral on the bonds is an interest in UTC's management contract with Navitech Services Corporation (see Note 12) and an interest in UTC's lease with Monroe County (see Note 4). UTC pays interest to the bank monthly at a variable rate as determined by the bank. Cash paid for interest was \$1,053,870 and \$1,142,369 in 2010 and 2009, respectively. Interest expense was \$1,130,293 and \$1,123,623 in 2010 and 2009, respectively.

The bond agreement requires a letter of credit to be maintained with the bank in the amount of \$24,825,480, of which \$24,490,000 is available to pay the principal on the bonds and \$335,480 is available to pay interest on the bonds. The letter of credit may be reduced as the outstanding principal is reduced. The letter of credit expires on March 31, 2017 at which time the Bonds will be callable unless an extension on the letter of credit is approved. The bonds are subject to mandatory sinking fund installments on March 1 of each year which commenced on March 1, 2007, and are used to repay the outstanding bonds and will continue annually each year until the outstanding principal amount of the bonds has been paid.

## 7. BONDS PAYABLE (Continued)

The schedule of sinking fund repayments is as follows:

<u>Payment Date</u>	<u>Installment</u>
March 1, 2011	\$ 2,100,000
March 1, 2012	2,200,000
March 1, 2013	2,240,000
March 1, 2014	2,345,000
March 1, 2015	2,455,000
March 1, 2016	2,575,000
March 1, 2017	2,650,000
March 1, 2018	2,670,000
March 1, 2019	2,685,000
March 1, 2020	<u>2,570,000</u>
	<u>\$ 24,490,000</u>

The Bonds contain a remarketing feature that permits the bonds to be remarketed on a weekly basis for purposes of resetting interest rates on the outstanding bonds. Failure of the Bonds to be remarketed would require the use of UTC's letter of credit to purchase any un-marketed bonds. In the event a tender advance is made on the letter of credit, UTC would be required to repay the bank subject to the terms of the agreement on demand.

### **Letter of Credit Covenants**

In connection with the letter of credit agreement, UTC is required to meet certain financial and operational covenants. As of December 31, 2010 and 2009, UTC was in compliance with these covenants. UTC's original maturity for the letter of credit agreement was March 2010. The letter of credit agreement was extended to 2017.

## 8. DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES

UTC has an interest rate swap which is qualified as a hedge under generally accepted accounting principles. As a result, the swap was recorded on the balance sheet at fair value. UTC had assumed no ineffectiveness in the swap due to the fact that, among other things, the notional amount of the swap was equal to the principal amount of the bonds and the variable rate that the UTC received under the swap matched the variable rate of the bonds. Changes in fair value of the swap have been accounted for in the statement of activities and change in net assets as a "gain or loss on interest rate swap agreement." The effective fixed interest rate of the swap was 3.8% during 2010 and 2009.

The fair value of the swap contract at December 31, 2010 and 2009 was a liability of \$1,900,669 and \$1,626,637, respectively. UTC is exposed to credit loss in the event of nonperformance by the other party to the interest rate swap contract. However, UTC does not anticipate nonperformance by the counterparty.

## 8. DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGING ACTIVITIES (Continued)

Fair value of UTC's derivative instrument at December 31 is as follows:

Derivative Instruments Designated as Hedging Instruments	Balance Sheet Location	Liability Derivatives	
		Fair Value	
		2010	2009
Interest rate swap	Long-term liability	\$ 1,900,669	\$ 1,626,637

The effect of derivative instruments on the statement of activities and change in net assets for the years ended December 31 consist of the following:

Derivatives in Fair Value Hedging Relationships	Location of Gain (Loss) Recognized in Change in Net Assets	Amount of Gain (Loss) Recognized in Change in Net Assets	
		2010	2009
		Interest rate swap	Other

## 9. FAIR VALUE MEASUREMENTS

The following are measured at fair value on a recurring basis at December 31, 2010:

Description	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
U.S. government money market funds	\$ 6,153,732	\$ -	\$ -
Mortgage-backed securities	-	579,948	-
	<u>\$ 6,153,732</u>	<u>\$ 579,948</u>	<u>\$ -</u>
Interest rate swap contract	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (1,900,669)</u>

## 9. FAIR VALUE MEASUREMENTS (Continued)

The following are measured at fair value on a recurring basis at December 31, 2009:

<u>Description</u>	<u>Level 1 Inputs</u>	<u>Level 2 Inputs</u>	<u>Level 3 Inputs</u>
U.S. government money market funds	\$ <u>6,089,075</u>	\$ _____ -	\$ _____ -
Interest rate swap contract	\$ _____ -	\$ _____ -	\$ <u>(1,626,637)</u>

The following is a reconciliation of the beginning and ending balances for UTC's interest rate swap contract measured at fair value on a recurring basis using significant unobservable inputs (Level 3):

	<u>2010</u>	<u>2009</u>
Balance at January 1	\$ (1,626,637)	\$ (2,247,810)
Unrealized gain (loss)	<u>(274,032)</u>	<u>621,173</u>
Balance at December 31	<u>\$ (1,900,669)</u>	<u>\$ (1,626,637)</u>

## 10. CAPITAL LEASE OBLIGATION

UTC has entered into a note payable agreement with a bank requiring quarterly payments of \$86,012, including interest at 4.6%, through January 2018. The related equipment collateralizes the capital lease obligation. This agreement allows UTC to purchase the leased equipment at the end of the lease term for \$1.

Future scheduled payments under this agreement are as follows for the years ending December 31:

2011	\$ 344,046
2012	344,046
2013	344,046
2014	344,046
2015	344,046
Thereafter	<u>774,104</u>
	2,494,334
Less: Amounts representing interest	(383,509)
Less: Current portion	<u>(251,241)</u>
	<u>\$ 1,859,584</u>

**11. OPERATING LEASE AGREEMENT**

UTC has leased copier equipment to Monroe County under the terms of an operating lease agreement commencing December 18, 2007 and terminating December 17, 2019. The annual lease payment also covers certain operating costs such as maintenance, technology upgrades, insurance, and management fees. The annual continuation of this agreement is solely dependent upon appropriations granted by Monroe County under the annual budgeting process and therefore is not guaranteed.

Future payments expected under this agreement are as follows for the years ending December 31:

2011	\$	925,627
2012		926,760
2013		927,916
2014		924,095
2015		925,297
Thereafter		<u>3,676,738</u>
	\$	<u>8,306,433</u>

**12. COMMITMENTS**

**Information Technology Services Agreement**

UTC previously entered into a long-term contract with Siemens Building Technologies (SBT) for management services related to technology and equipment management. On January 1, 2009 SBT assigned this contract with UTC to Navitech Services Corporation (Navitech), an unrelated third party. The agreement commenced on February 7, 2005 and terminates on February 7, 2013 with two consecutive four-year renewal options. UTC is required to pay Navitech an annual fee in two installments each year on February 15 and August 15. The management fee was \$389,676 in 2010 and 2009. The management fee is based on the lower of 2% or the Consumer Price Index – U, Northeast Region. Future payments under this agreement are as follows for the years ending December 31:

2012	\$	397,470
2013		<u>405,419</u>
	\$	<u>802,889</u>

**12. COMMITMENTS (Continued)**

**Copier Services Agreement**

In December 2007, as an addendum to the long-term contract originally with SBT, UTC had contracted with SBT to provide services to coordinate the management, provision and installation of copier equipment and software. The agreement commenced on December 19, 2007 and terminated on December 18, 2010, but was renewed for another three years. This agreement has two additional consecutive three-year renewal options. The management fee recognized was \$55,539 and \$54,450 in 2010 and 2009, respectively. As of January 1, 2009 SBT assigned this contract with UTC to Navitech. All terms of the contract remain unchanged over the remaining contract period. UTC will pay Navitech an annual fee in two installments each year on January 15 and July 15. Future payments under this agreement are as follows for the years ending December 31:

2011	\$	56,650
2012		57,783
2013		<u>58,938</u>
	\$	<u>173,371</u>

**13. SUBSEQUENT EVENTS**

Subsequent events have been evaluated through March 21, 2011, which is the date the financial statements were issued.

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

March 21, 2011

To the Board of Directors of  
Upstate Telecommunications Corporation:

We have audited the financial statements of Upstate Telecommunications Corporation (UTC), a New York nonprofit organization, as of and for the year ended December 31, 2010, and have issued our report thereon dated March 21, 2011. We conducted our audit in accordance with auditing standards generally accepted in the United States 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 UTC'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 UTC's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of UTC's internal control over financial reporting.

*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.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

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

(Continued)

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether UTC'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 management, the audit committee, Board of Directors, and others within the entity and is not intended to be and should not be used by anyone other than these specified parties.