

YEAR ENDING \_\_\_\_\_ 2008  
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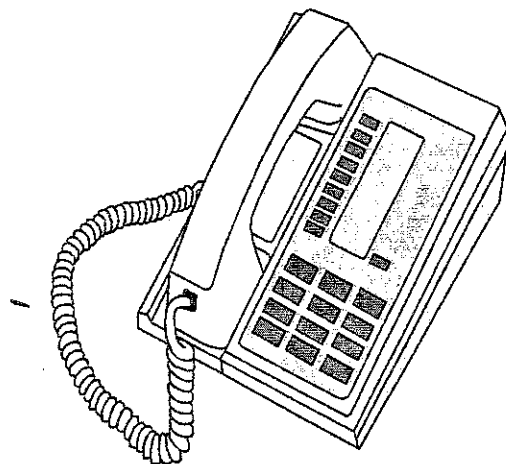
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PUBLIC SERVICE  
COMMISSION

# ANNUAL REPORT OF

SOUTHERN MONTANA TELEPHONE Co.

## TELEPHONE UTILITY



TO THE  
PUBLIC SERVICE COMMISSION  
STATE OF MONTANA  
1701 PROSPECT AVENUE  
P.O. BOX 202601  
HELENA, MT 59620-2601

**General Information**

Year: 2008

1	Legal Name of Respondent:	Southern Montana Telephone Company
2	Name Under Which Respondent Does Business:	Southern Montana Telephone Company
3	Date of Incorporation:	1944
4	Address to send Correspondence Concerning Report:	P.O. Box 205 Wisdom MT 59761-
5	Person Responsible for This Report:	Rick Knight, Office Manager
5a.	Telephone Number:	406-689-3333
<b>Control Over Respondent</b>		
1	If direct control over the respondent was held by another entity at the end of year provide the following:	
	1a. Name and address of the controlling organization or person:	
	1b. Means by which control was held:	
	1c. Percent Ownership:	

<b>Board of Directors</b>		
Line No.	Name of Director and Address (City, State) (a)	Fees Paid During Year (b)
1	Robert G. Helming Wisdom, MT	9000
2	Tara E. Helming Wisdom, MT	9000
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18	<b>Chairman of the Board:</b> Robert G. Helming	
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**Officers**

Year: 2008

Line No.	Title of Officer (a)	Department Over Which Jurisdiction is Exercised (b)	Name and Address of Person Holding Office at Year End (c)
1	President	All Departments	Robert G. Helming
2			Wisdom MT 59761
3			
4			
5	Secretary/Treasurer	All Departments	Tara E. Helming
6			Wisdom, MT 59761
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**Total Company Balance Sheet**

Year: 2008

Line No.	Acct. No. (a)	Description (b)	This Year (c)	Last Year (d)
1		<b>CURRENT ASSETS:</b>		
2	1120	Cash and Equivalents	See Attached AUDITED Financials	
3	1180	Telecommunications Accounts Receivable - Net		
4	1190	Other Accounts Receivable - Net		
5	1200	Notes Receivable - Net		
6	1210	Interest and Dividends Receivable		
7	1220	Materials and Supplies		
8	* 1280	Prepayments		
9	^ 1290	Prepaid Rents		
10	^ 1300	Prepaid Taxes		
11	^ 1310	Prepaid Insurance		
12	^ 1320	Prepaid Directory Expenses		
13	^ 1330	Other Prepayments		
14	1350	Other Current Assets		
15		<b>Total Current Assets</b>		
16		<b>NONCURRENT ASSETS:</b>		
17	1401	Investments in Affiliated Companies		
18	1402	Investments in Nonaffiliated Companies		
19	1406	Nonregulated Investments		
20	1407	Unamortized Debt Issuance Expense		
21	1408	Sinking Funds		
22	1410	Other Noncurrent Assets		
23	1438	Deferred Maintenance and Retirements		
24	1439	Deferred Charges		
25	1500	Other Jurisdictional Assets - Net		
26		<b>Total Noncurrent Assets</b>		
27		<b>PROPERTY, PLANT, &amp; EQUIPMENT:</b>		
28	2001	Telecommunications Plant in Service		
29	2002	Property Held for Future Telecommunications Use		
30	2003	Plant Under Construction - Short Term		
31	2004	Plant Under Construction - Long Term		
32	2005	Telecommunications Plant Adjustment		
33	2006	Nonoperating Plant		
34	2007	Goodwill		
35	3100	Accumulated Depreciation		
36	3200	Accumulated Depreciation - Held for Future Use		
37	3300	Accumulated Depreciation - Nonoperating		
38	3400	Accumulated Amortization		
39		<b>Net Property, Plant, &amp; Equipment</b>		
40		<b>TOTAL ASSETS</b>		

^ Subaccount of account marked with a \*.

# SOUTHERN MONTANA TELEPHONE COMPANY

## Balance Sheets

December 31, 2008 and 2007

<b>ASSETS</b>	<u>2008</u>	<u>2007</u>
Current Assets:		
Cash and cash equivalents	\$ 1,806,514	\$ 1,889,500
Marketable securities	-	40,000
Accounts receivable, less allowance for doubtful accounts of \$16,057 (\$20,266 in 2007)	283,129	363,755
Materials and supplies	63,625	63,538
Prepaid expenses	<u>28,048</u>	<u>4,900</u>
Total Current Assets	<u>2,181,316</u>	<u>2,361,693</u>
Other investments	352,501	351,067
Property, Plant, and Equipment:		
In-service	12,475,685	11,180,524
Under construction	<u>2,013,665</u>	<u>367,366</u>
	14,489,350	11,547,890
Less accumulated depreciation	<u>6,642,614</u>	<u>5,971,996</u>
Property, Plant, and Equipment, net	<u>7,846,736</u>	<u>5,575,894</u>
	<u>\$ 10,380,553</u>	<u>\$ 8,288,654</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities:		
Current portion of long-term debt	\$ 282,221	\$ 304,936
Accounts payable	68,662	129,539
Advance billing and customer deposits	16,076	27,663
Accrued expenses	<u>388,253</u>	<u>192,833</u>
Total Current Liabilities	<u>755,212</u>	<u>654,971</u>
Long-Term Debt	<u>5,945,186</u>	<u>3,738,976</u>
Stockholders' Equity:		
Common stock, \$10 par value, 2,703 shares authorized and 610 shares issued and outstanding	6,100	6,100
Paid-in capital	3,290	3,290
Retained earnings	<u>3,670,765</u>	<u>3,885,317</u>
Total Stockholders' Equity	<u>3,680,155</u>	<u>3,894,707</u>
	<u>\$ 10,380,553</u>	<u>\$ 8,288,654</u>

See accompanying notes to consolidated financial statements.

**Total Company Balance Sheet**

Year: 2008

Line No.	Acct. No. (a)	Description (b)	This Year (c)	Last Year (d)
41		<b>CURRENT LIABILITIES:</b>		
42	4010	Accounts Payable		
43	4020	Notes Payable		
44	4030	Advance Billing and Payments		
45	4040	Customer Deposits		
46	4050	Current Maturities - Long Term Debt		
47	4060	Current Maturities - Capital Leases		
48	4070	Income Taxes - Accrued		
49	4080	Other Taxes - Accrued		
50	4100	Net Current Deferred Operating Income Taxes		
51	4110	Net Current Deferred Nonoperating Income Taxes		
52	4120	Other Accrued Liabilities		
53	4130	Other Current Liabilities		
54		<b>Total Current Liabilities</b>		
55		<b>LONG-TERM DEBT:</b>		
56	4210	Funded Debt		
57	4220	Premium on Long-Term Debt		
58	4230	Discount on Long-Term Debt		
59	4240	Reacquired Debt		
60	4250	Obligations Under Capital leases		
61	4260	Advances From Affiliated Companies		
62	4270	Other Long-Term Debt		
63		<b>Total Long-Term Debt</b>		
64		<b>OTHER LIABILITIES AND DEFERRED CREDITS:</b>		
65	4310	Other Long-Term Liabilities		
66	4320	Unamort. Oper. Invest. Tax Credits - Net		
67	4330	Unamort. Nonoper. Invest. Tax Credits - Net		
68	4340	Net Noncurrent Deferred Oper. Income Taxes		
69	4350	Net Noncurrent Deferred Nonoper. Income Taxes		
70	4360	Other Deferred Credits		
71	4370	Other Jurisdictional Liab. and Def. Credits		
72		<b>Total Other Liabilities and Deferred Credits</b>		
73		<b>STOCKHOLDERS' EQUITY:</b>		
74	4510	Capital Stock		
75	4520	Additional Paid-In Capital		
76	4530	Treasury Stock		
77	4540	Other Capital		
78	4550	Retained Earnings		
79		<b>Total Stockholders' Equity</b>		
80		<b>TOTAL LIAB. AND STOCKHOLDERS' EQUITY</b>		

**SOUTHERN MONTANA TELEPHONE COMPANY****Balance Sheets**

December 31, 2008 and 2007

<b>ASSETS</b>	<u>2008</u>	<u>2007</u>
Current Assets:		
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Marketable securities	-	40,000
Accounts receivable, less allowance for doubtful accounts of \$16,057 (\$20,266 in 2007)	283,129	363,755
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Under construction	<u>2,013,665</u>	<u>367,366</u>
	14,489,350	11,547,890
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Total Stockholders' Equity	<u>3,680,155</u>	<u>3,894,707</u>
	<u>\$ 10,380,553</u>	<u>\$ 8,288,654</u>

See accompanying notes to consolidated financial statements.

**Total Company Income Statement**

Year: 2008

Line No.	Acct. No. (a)	Description (b)	This Year (c)	Last Year (d)	
1		<b>REVENUES:</b>			
2	5000	Basic Local Service Revenues			
3	5080	Network Access Revenues			
4	* 5100	Long Distance Message Revenue			
5	^ 5110	Unidirectional Long Distance Revenue	See Attached AUDITED Financials		
6	^ 5120	Long Distance Private Network Revenue			
7	^ 5160	Other Long Distance Revenue			
8	^ 5169	Other Long Distance Revenue Settlements			
9	* 5200	Miscellaneous Revenue			
10	^ 5230	Directory Revenue			
11	^ 5240	Rent Revenue			
12	^ 5250	Corporate Operations Revenue			
13	^ 5260	Miscellaneous Revenue			
14	^ 5270	Carrier Billing and Collection Revenue			
15	^ 5280	Nonregulated Revenue			
16	5300	Uncollectible Revenue			
17		<b>Total Revenues (L.2+L.3+L.4+L.9-L.16)</b>			
18		<b>OPERATING EXPENSES:</b>			
19	6110	Network Support Expense			
20	6120	General Support Expense			
21	6210	Central Office Switching Expense			
22	6220	Operator Systems Expense			
23	6230	Central Office Transmission Expense			
24	6310	Information Origination/Termination Expense			
25	* 6410	Cable and Wire Facilities Expense			
26	^ 6431	Aerial Wire Expense			
27	^ 6441	Conduit Systems Expense			
28	6510	Other Property, Plant & Equipment Expense			
29	6530	Network Operations Expense			
30	6540	Access Expense			
31	6560	Depreciation and Amortization Expense			
32	6610	Marketing			
33	6620	Services			
34	6710	Executive and Planning			
35	6720	General and Administrative			
36	6790	Provision for Uncollectible Notes Receivable			
37		<b>Total Operating Expenses (Sum L.19 to L.36-L.26-L.27)</b>			
38	7100	Other Operating Income and Expense			
39	7200	Operating Taxes			
40		<b>Net Operating Income (L.17-L.37+L.38-L.39)</b>			
41	7300	Nonoperating Income and Expense			
42	7400	Nonoperating Taxes			
43	7500	Interest and Related Items			
44	7600	Extraordinary Items			
45	7910	Effects of Juris. Ratemaking Diff. - Net			
46	7990	Nonregulated Net Income			
47		<b>NET INCOME (L.40+L.41-L.42-L.43-L.44+L.45-L.46)</b>			

^ Subaccount of the account marked with a \*.



# SOUTHERN MONTANA TELEPHONE COMPANY

## Statements of Income

Years Ended December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Operating Revenues:		
Local network	\$ 178,843	\$ 186,274
Interstate access	1,919,946	1,736,981
Intrastate access	470,949	405,697
Miscellaneous	<u>5,366</u>	<u>3,772</u>
Total Operating Revenues	<u>2,575,104</u>	<u>2,332,724</u>
Operating Expenses:		
Plant specific operations	407,169	483,618
Plant nonspecific operations	180,703	299,760
Customer	67,635	53,034
Corporate	874,999	586,597
Depreciation and amortization	675,903	597,798
Other operating taxes	63,359	46,986
Nonregulated, net	<u>135,554</u>	<u>71,649</u>
Total Operating Expenses	<u>2,405,322</u>	<u>2,139,442</u>
Operating Income	169,782	193,282
Other Income (Expense):		
Other Income (Expense)	(93,827)	97,410
Allowance for funds used during construction	<u>39,674</u>	<u>15,248</u>
Total Other Income (Expense)	<u>(54,153)</u>	<u>112,658</u>
Income Available for Fixed Charges	115,629	305,940
Fixed Charges - Interest on Long-Term Debt	<u>189,695</u>	<u>91,589</u>
Net Income (Loss)	<u>\$ (74,066)</u>	<u>\$ 214,351</u>

## Montana Total State Income Statement

Year: 2008

Line No.	Acct. No. (a)	Description (b)	This Year (c)	Last Year (d)
1		<b>REVENUES:</b>		
2	5000	Basic Local Service Revenues		
3	5080	Network Access Revenues		
4	* 5100	Long Distance Message Revenue		
5	^ 5110	Unidirectional Long Distance Revenue	Not Applicable	
6	^ 5120	Long Distance Private Network Revenue		
7	^ 5160	Other Long Distance Revenue		
8	^ 5169	Other Long Distance Revenue Settlements		
9	* 5200	Miscellaneous Revenue		
10	^ 5230	Directory Revenue		
11	^ 5240	Rent Revenue		
12	^ 5250	Corporate Operations Revenue		
13	^ 5260	Miscellaneous Revenue		
14	^ 5270	Carrier Billing and Collection Revenue		
15	^ 5280	Nonregulated Revenue		
16	5300	Uncollectible Revenue		
17		<b>Total Revenues (L.2+L.3+L.4+L.9-L.16)</b>		
18		<b>OPERATING EXPENSES:</b>		
19	6110	Network Support Expense		
20	6120	General Support Expense		
21	6210	Central Office Switching Expense		
22	6220	Operator Systems Expense		
23	6230	Central Office Transmission Expense		
24	6310	Information Origination/Termination Expense		
25	* 6410	Cable and Wire Facilities Expense		
26	^ 6431	Aerial Wire Expense		
27	^ 6441	Conduit Systems Expense		
28	6510	Other Property, Plant & Equipment Expense		
29	6530	Network Operations Expense		
30	6540	Access Expense		
31	6560	Depreciation and Amortization Expense		
32	6610	Marketing		
33	6620	Services		
34	6710	Executive and Planning		
35	6720	General and Administrative		
36	6790	Provision for Uncollectible Notes Receivable		
37		<b>Total Operating Expenses (Sum L.19 to L.36-L.26-L.27)</b>		
38	7100	Other Operating Income and Expense		
39	7200	Operating Taxes		
40		<b>Net Operating Income (L.17-L.37+L.38-L.39)</b>		

^ Subaccount of the account marked with a \*.

**Montana Intrastate Income Statement**

Year: 2008

Line No.	Acct. No. (a)	Description (b)	This Year (c)	Last Year (d)
1		<b>REVENUES:</b>		
2	5000	Basic Local Service Revenues		
3	5080	Network Access Revenues		
4	* 5100	Long Distance Message Revenue		
5	^ 5110	Unidirectional Long Distance Revenue	Not Applicable	
6	^ 5120	Long Distance Private Network Revenue		
7	^ 5160	Other Long Distance Revenue		
8	^ 5169	Other Long Distance Revenue Settlements		
9	* 5200	Miscellaneous Revenue		
10	^ 5230	Directory Revenue		
11	^ 5240	Rent Revenue		
12	^ 5250	Corporate Operations Revenue		
13	^ 5260	Miscellaneous Revenue		
14	^ 5270	Carrier Billing and Collection Revenue		
15	^ 5280	Nonregulated Revenue		
16	5300	Uncollectible Revenue		
17		<b>Total Revenues (L.2+L.3+L.4+L.9-L.16)</b>		
18		<b>OPERATING EXPENSES:</b>		
19	6110	Network Support Expense		
20	6120	General Support Expense		
21	6210	Central Office Switching Expense		
22	6220	Operator Systems Expense		
23	6230	Central Office Transmission Expense		
24	6310	Information Origination/Termination Expense		
25	* 6410	Cable and Wire Facilities Expense		
26	^ 6431	Aerial Wire Expense		
27	^ 6441	Conduit Systems Expense		
28	6510	Other Property, Plant & Equipment Expense		
29	6530	Network Operations Expense		
30	6540	Access Expense		
31	6560	Depreciation and Amortization Expense		
32	6610	Marketing		
33	6620	Services		
34	6710	Executive and Planning		
35	6720	General and Administrative		
36	6790	Provision for Uncollectible Notes Receivable		
37		<b>Total Operating Expenses (Sum L.19 to L.36-L.26-L.27)</b>		
38	7100	Other Operating Income and Expense		
39	7200	Operating Taxes		
40		<b>Net Operating Income (L.17-L.37+L.38-L.39)</b>		

^ Subaccount of the account marked with a \*.

**Montana Intrastate Regulated Income Statement**

Year: 2008

Line No.	Acct. No. (a)	Description (b)	This Year (c)	Last Year (d)	
1		<b>REVENUES:</b>			
2	5000	Basic Local Service Revenues			
3	5080	Network Access Revenues			
4	* 5100	Long Distance Message Revenue	Not Applicable		
5	^ 5110	Unidirectional Long Distance Revenue			
6	^ 5120	Long Distance Private Network Revenue			
7	^ 5160	Other Long Distance Revenue			
8	^ 5169	Other Long Distance Revenue Settlements			
9	* 5200	Miscellaneous Revenue			
10	^ 5230	Directory Revenue			
11	^ 5240	Rent Revenue			
12	^ 5250	Corporate Operations Revenue			
13	^ 5260	Miscellaneous Revenue			
14	^ 5270	Carrier Billing and Collection Revenue			
15	^ 5280	Nonregulated Revenue			
16	5300	Uncollectible Revenue			
17		<b>Total Revenues (L.2+L.3+L.4+L.9-L.16)</b>		#VALUE!	
18		<b>OPERATING EXPENSES:</b>			
19	6110	Network Support Expense			
20	6120	General Support Expense			
21	6210	Central Office Switching Expense			
22	6220	Operator Systems Expense			
23	6230	Central Office Transmission Expense			
24	6310	Information Origination/Termination Expense			
25	* 6410	Cable and Wire Facilities Expense			
26	^ 6431	Aerial Wire Expense			
27	^ 6441	Conduit Systems Expense			
28	6510	Other Property, Plant & Equipment Expense			
29	6530	Network Operations Expense			
30	6540	Access Expense			
31	6560	Depreciation and Amortization Expense			
32	6610	Marketing			
33	6620	Services			
34	6710	Executive and Planning			
35	6720	General and Administrative			
36	6790	Provision for Uncollectible Notes Receivable			
37		<b>Total Operating Expenses (Sum L.19 to L.36-L.26-L.27)</b>			
38	7100	Other Operating Income and Expense			
39	7200	Operating Taxes			
40		<b>Net Operating Income (L.17-L.37+L.38-L.39)</b>	#VALUE!		

^ Subaccount of the account marked with a \*.

## Average Rate Base - Total State

Year: 2008

Line No.	Acct. No. (a)	Description (b)	This Year (c)	Last Year (d)
1	2001	Telecommunications Plant in Service		
2	3100	Accumulated Depreciation		
3	2002	Property Held for Future Telecommunications Use		
4	3200	Accumulated Depreciation - 2002		
5	1220	Materials and Supplies		
6	4340	Noncurrent Deferred Operating Income Taxes		
7		Pre-1971 Unamortized Investment Tax Credits		
8		Cash Working Capital (if allowed by Commission)		
9		<b>Total Average Rate Base (L.1-L.2+L.3-L.4+L.5-L.6-L.7+L.8)</b>		

## Average Rate Base - Intrastate

Line No.	Acct. No. (a)	Description (b)	This Year (c)	Last Year (d)
1	2001	Telecommunications Plant in Service		
2	3100	Accumulated Depreciation		
3	2002	Property Held for Future Telecommunications Use		
4	3200	Accumulated Depreciation - 2002		
5	1220	Materials and Supplies		
6	4340	Noncurrent Deferred Operating Income Taxes		
7		Pre-1971 Unamortized Investment Tax Credits		
8		Cash Working Capital (if allowed by Commission)		
9		<b>Total Average Rate Base (L.1-L.2+L.3-L.4+L.5-L.6-L.7+L.8)</b>		

## Average Rate Base - Regulated Intrastate

Line No.	Acct. No. (a)	Description (b)	This Year (c)	Last Year (d)
1	2001	Telecommunications Plant in Service	14489350	
2	3100	Accumulated Depreciation	6642614	
3	2002	Property Held for Future Telecommunications Use		
4	3200	Accumulated Depreciation - 2002		
5	1220	Materials and Supplies	63625	
6	4340	Noncurrent Deferred Operating Income Taxes		
7		Pre-1971 Unamortized Investment Tax Credits		
8		Cash Working Capital (if allowed by Commission)		
9		<b>Total Average Rate Base (L.1-L.2+L.3-L.4+L.5-L.6-L.7+L.8)</b>	7910361	

## Statement of Cash Flows

Year: 2008

Line No.	Item Description (a)	Amount (b)	Amount (c)
1	<b>Increase/(decrease) in Cash &amp; Cash Equivalents</b>		
2	<b>Cash Flows from Operating Activities:</b>		
3	Net Income		
4	Reconciliation Adjustments:		
5	Depreciation & Amortization		
6	Provision for Accounts Receivable Losses		
7	Deferred Income Taxes - Net		
8	Unamortized Investment Tax Credits (ITCs) - Net		
9	Allowance for Funds Used During Construction (AFUDC)	See ATTACHED STATEMENT	
10	Change in Operating Receivables - Net	OF CASH FLOWS	
11	Change in Materials, Supplies & Inventories - Net		
12	Change in Operating Payables & Accrued Liabilities - Net		
13	Change in Other Assets & Deferred Credits - Net		
14	Change in Other Liabilities & Deferred Credits - Net		
15	Other (explained on back of this page)		
16	Total Adjustments		
17	<b>Net Cash Provided by/(Used in) Operating Activities</b>		
18	<b>Cash Inflows/Outflows From Investing Activities:</b>		
19	Construction/Acquisition of Property, Plant & Equipment (net of		
20	AFUDC & Capital Lease Related Acquisitions)		
21	Proceeds from Disposals of Property, Plant & Equipment		
22	Investments In & Advances to Affiliates		
23	Proceeds from Repayment of Advances		
24	Other Investing Activities (explained on back of this page)		
25	<b>Net Cash Provided by/(Used in) Investing Activities</b>		
26	<b>Cash Flows from Financing Activities:</b>		
27	Net Incr./((Decr.) in Short-Term Debt, Original maturity <= 3 mo.		
28	Advances from Affiliates		
29	Repayment of Advances from Affiliates		
30	Proceeds from Issuances of Long-Term Debt		
31	Repayment of Long-Term Debt		
32	Payment of Capital Lease Obligations		
33	Proceeds from Issuing Common Stock/Parent Co. Equity Investment		
34	Repurchase of Treasury Shares		
35	Dividends Paid		
36	Other Financing Activities (explained on back of this page)		
37	<b>Net Cash Provided by Financing Activities</b>		
38	<b>Effect of Exchange Rate Changes on Cash</b>		
39	<b>Net Increase/(Decrease) in Cash &amp; Cash Equivalents</b>		
40	<b>Cash &amp; Cash Equivalents at Beginning of Period</b>		
41	<b>Cash &amp; Cash Equivalents at End of Period</b>		

**SOUTHERN MONTANA TELEPHONE COMPANY****Statements of Cash Flows**

Years Ended December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Cash Flows from Operating Activities:		
Net income (loss)	\$ (74,066)	\$ 214,351
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	675,903	597,798
Patronage capital credits, noncash	-	(16,668)
Realized (gain) loss on sale of marketable securities	-	(15,495)
Changes in assets and liabilities:		
Accounts receivable	80,626	28,254
Materials and supplies	(87)	(7,111)
Prepaid expenses	(23,148)	1,792
Accounts payable	(60,877)	(150,556)
Advance billing and customer deposits	(11,587)	(9,495)
Accrued expenses	195,420	(5,299)
Net Cash Provided by Operating Activities	<u>782,184</u>	<u>637,571</u>
Cash Flows from Investing Activities:		
Capital expenditures	(2,946,745)	(2,733,712)
Purchase of other investments	-	(1,191,482)
Proceeds from sale of marketable securities and investments	38,566	1,441,497
Net Cash Used by Investing Activities	<u>(2,908,179)</u>	<u>(2,483,697)</u>
Cash Flows from Financing Activities:		
Proceeds from long-term debt	2,413,061	3,380,129
Payments on long-term debt	(229,566)	(1,118,880)
Equity distributions	(140,486)	(139,540)
Net Cash Provided by Financing Activities	<u>2,043,009</u>	<u>2,121,709</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(82,986)	275,583
Cash and Cash Equivalents, beginning	<u>1,889,500</u>	<u>1,613,917</u>
Cash and Cash Equivalents, ending	<u>\$ 1,806,514</u>	<u>\$ 1,889,500</u>
Cash Paid During the Year for Interest, net of amount capitalized	<u>\$ 150,021</u>	<u>\$ 76,341</u>

See accompanying notes to consolidated financial statements.

Receivables and Investments-Affiliated & Nonaffiliated Companies

Year: 2008

Line No.	Name of Affiliate or Company (a)	Account 1160 Temporary Investments (b)	Account 1180 Telecom. Accounts Receivable (c)	Account 1181 Accts. Rec. Telecom. Allowance (d)	Account 1190 Other Accounts Receivable (e)	Account 1191 Accounts Receivable flow. - Other (f)	Account 1200 Notes Receivable (g)	Account 1201 Notes Receivable Allowance (h)	Account 1210 Interest and Dividends Receivable (i)	Account 1401 Investments in Affil. Companies (j)	Account 1402 Investments in Nonaffil. Companies (k)
1	Telecom Customers		61461		207361				3208		264106 73510
2	Vision Net Investment										
3	Various										
4											
5											
6											
7											
8											
9											
10											
11											
12											
13											
14											
15											
16											
17											
18											
19											
20											
21											
22											
23											
24											
25											
26											
27											
28											
29											
30	<b>Totals</b>		61461		207361				3208		337616



Net Plant in Service - Detail

Year: 2008

Line No.	Account (a)	Description (b)	Beginning of Year Balance (c)	Additions (d)	Retirements (e)	Sales & Transfers (f)	End of Year Account 2001 Balance (g)	Year End Accumulated Depreciation (h)	End of Year Net Plant Balance (i)
1	*	2110 Land and Support Assets	1479607	44399	21063		1503763	1231247	272516
2	^	2111 Land	38451				38451		38451
3	^	2112 Motor Vehicles	276283		21063		255220	271221	-16001
4	^	2113 Aircraft							
5	^	2114 Special Purpose Vehicles							
6	^	2115 Garage Work Equipment							
7	^	2116 Other Work Equipment	467578				467578	470897	-3319
8	^	2121 Buildings	629513	28625			658957	441991	216966
9	^	2122 Furniture	41295				41296	23261	18035
10	^	2123 Office Equipment							
11	^	2124 General Purpose Computers	26487	15774			42261	23877	18384
12		2211 Analog Electronic Switching							
13		2212 Digital Electronic Switching	1311167	72139	8979		1376392	1111085	265307
14		2215 Electro-Mechanical Switching							
15		2220 Operator Systems							
16		2231 Radio Systems							
17		2232 Circuit Equipment	1457758	272147			1737695	790121	947574
18	*	2310 Information Orig & Term Equip	22595				22595	18527	4068
19	^	2311 Station Apparatus	18527				18527	18527	
20	^	2321 Customer Premises Wiring							
21	^	2341 Large Private Branch Exchanges	4068				4068		4068
22	^	2351 Public Telephone Term. Equip.							
23	^	2362 Other Terminal Equipment							
24		2411 Poles							
25	*	2420 Cable and Wire Facilities	33375				33375	22717	10658
26	^	2421 Aerial Cable							
27	^	2422 Underground Cable							
28	^	2423 Buried Cable	6875798	926067			7801865	3468917	4332948
29	^	2424 Submarine Cable							
30	^	2425 Deep Sea Cable							
31	^	2426 Intrabuilding Network Cable							
32		2431 Aerial Wire							
33		2441 Conduit Systems							
34		<b>Totals</b>	11180300	1314752	30042		12475685	6642614	5833071

^ Subaccount of the account marked with a \*

**Analysis of Plant Held for Future Use**

Year: 2008

Line No.	Location and Description of Property (a)	Date Included in Account 2002 (b)	Book Cost of Property at Beginning of Year (c)	Additions During the Year (d)	Retirements During the Year (e)	Transfers and Adjustments Charges and (Credits) (f)	Book Cost of Property at End of Year (g)
1							
2	None						
3							
4							
5							
6							
7							
8							
9							
10							
11							
12							
13							
14							
15							
16							
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18							
19							
20							
21							
22							
23							
24							
25							
26							
27							
28							
29							
30	<b>Totals</b>						

(Sum L. 1 to L.29)

Average Cost of Long Term Debt

Year: 2008

Line No.	Description (a)	Issue Date (b)	Maturity Date (c)	Principal Amount (d)	Gross Proceeds (e)	Net Proceeds (f)	Net Per \$100 (g)	Outstanding Per Balance Sheet (h)	Yield to Maturity (i)	Annual Net Cost (j)	Amortization of Premium or Discount (k)	Total Cost (%) (l)
1	Note Payable	"2000	"2010.	665000				143744		13312		7.50%
2												
3	USDA-RUS	Various	Various	4087000				1190468		169624		2.00%
4												
5	USDA-RUS	"2008	"2026	2480134				2480134		118788		4.6-4.8%
6												
7												
8	USDA-RUS	"2008	"2026	2413061				2413061		110518		2.692--4.58%
9												
10												
11												
12												
13												
14												
15												
16												
17												
18												
19												
20												
21												
22												
23												
24												
25												
26												
27												
28												
29												
30	<b>Total</b>			9645195				6227407		412242		6.62%

**Cost of Preferred Stock**

Year: 2008

Line No.	Description (a)	Date of Issuance (b)	Method of Offering (c)	Call Redemption Price (d)	Par Value Of Issue (e)	Gross Proceeds Amounts (f)	Net Proceeds Amounts (g)	Net Proceeds Per \$100 (h)	Cost of Money (i)	Principal Outstanding (j)	Annual Cost (k)	Embedded Cost (l)
1												
2	NONE											
3												
4												
5												
6												
7												
8												
9												
10												
11												
12												
13												
14												
15												
16												
17												
18												
19												
20												
21												
22												
23												
24												
25												
26												
27												
28												
29												
30	<b>Totals (Sum L. 1 to L.29)</b>											

Analysis of Common Stock

Year: 2008

Line No.	(a)	Avg. Number of Shares Outstanding (b)	Book Value (per share) (c)	Earnings (per share) (d)	Dividends (per share) (e)	Retention Ratio (f)	Market Price High (g)	Market Price Low (h)	Price/Earnings Ratio (i)
1	Year Ended December 31:								
2									
3									
4									
5	This stock is privately held, there is no market for this stock.								
6									
7									
8	Month by Month Data:								
9	January								
10	February								
11	March								
12	April								
13	May								
14	June								
15	July								
16	August								
17	September								
18	October								
19	November								
20	December								
21									
22									
23									

**SOUTHERN MONTANA TELEPHONE COMPANY**  
**Statements of Changes in Stockholders' Equity**  
Years Ended December 31, 2008 and 2007

	Capital Stock		Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total
	Shares Issued	Amount				
Balance, December 31, 2006	610	\$ 6,100	\$ 3,290	\$ 3,810,506	\$ (10,605)	\$ 3,809,291
Change in unrealized loss on available for sale securities	-	-	-	-	26,100	26,100
Reclassification adjustment	-	-	-	-	(15,495)	(15,495)
Distributions	-	-	-	(139,540)	-	(139,540)
Net income	-	-	-	214,351	-	214,351
Balance, December 31, 2007	610	6,100	3,290	3,885,317	-	3,894,707
Distributions	-	-	-	(140,486)	-	(140,486)
Net loss	-	-	-	(74,066)	-	(74,066)
Balance, December 31, 2008	<u>610</u>	<u>\$ 6,100</u>	<u>\$ 3,290</u>	<u>3,670,765</u>	<u>\$ -</u>	<u>\$ 3,680,155</u>

See accompanying notes to consolidated financial statements.

**Capital Stock and Funded Debt Reacquired or Retired During the Year**

Year: 2008

Line No.	Description of Security (a)	Call or Retirement Date (b)	Number of Shares (c)	Principal Amount (d)	Reacquisition or Retirement Cost (e)	Gain or (Loss) (f)	Retirement or Reacquisition (g)
1							
2							
3							
4							
5							
6							
7	N/A						
8							
9							
10							
11							
12							
13							
14							
15							
16							
17							
18							
19							
20							
21							
22							
23							
24							
25							
26							
27							
28							
29							
30	<b>Totals (Sum L.1 to L.29)</b>						

**Total Company Expense Matrix**

Line No.	Acct. No. (a)	Description (b)	Salaries and Wages (c)	Benefits (d)	Rents (e)	Other Expenses (f)	Clearances (g)	Total (h)
1	* 6110	Network Support Expense						
2	^ 6112	Motor Vehicle Expense						
3	^ 6113	Aircraft Expense						
4	^ 6114	Special Purpose Vehicles Expense						
5	^ 6115	Garage Work Equipment Expense						
6	^ 6116	Other Work Equipment Expense						
7	* 6120	General Support Expense						
8	^ 6121	Land and Building Expense						
9	^ 6122	Furniture and Artworks Expense						
10	^ 6123	Office Equipment Expense						
11	^ 6124	General Purpose Computers Expense						
12	* 6210	Central Office Switching Expense						
13	^ 6211	Analog Electronic Expense						
14	^ 6212	Digital Electronic Expense						
15	^ 6215	Electro-Mechanical Expense						
16	6220	Operator Systems Expense						
17	* 6230	Central Office Transmission Expense						
18	^ 6231	Radio Systems Expense						
19	^ 6232	Circuit Equipment Expense						
20	* 6310	Information Origination/Termination Expense						
21	^ 6311	Station Apparatus Expense						
22	^ 6341	Large Private Branch Exchange Expense						
23	^ 6351	Public Telephone Terminal Equipment Exp.						
24	^ 6362	Other Terminal Equipment Expense						
25	* 6410	Cable and Wire Facilities Expense						
26	^ 6411	Poles Expense						
27	^ 6421	Aerial Cable Expense						
28	^ 6422	Underground Cable Expense						
29	^ 6423	Buried Cable Expense						
30	^ 6424	Submarine Cable Expense						
31	^ 6425	Deep Sea Cable Expense						
32	^ 6426	Intrabuilding Network Cable Expense						
33	^ 6431	Aerial Wire Expense						
34		<b>Subtotals</b>						

^ Subaccount of the account marked with a \*.



**Total Company Expense Matrix**

Line No.	Acct. No. (a)	Description (b)	Salaries and Wages (c)	Benefits (d)	Rents (e)	Other Expenses (f)	Clearances (g)	Total (h)
35	^ 6441	Conduit Systems Expense						
36	6510	Other Property Expenses						
37	* 6530	Network Operations Expense						
38	^ 6531	Power Expense						
39	^ 6532	Network Administration Expense						
40	^ 6533	Testing Expense						
41	^ 6534	Plant Operations Expense						
42	^ 6535	Engineering Expense						
43	6540	Access Expense						
44	6561	Depreciation - Telecomm. Plant in Service						
45	6562	Depreciation-Prop. for Future Telecom. Use						
46	6563	Amortization Expense - Tangible						
47	6564	Amortization Expense - Intangible						
48	6565	Amortization - Other						
49	* 6610	Marketing						
50	^ 6611	Product Management						
51	^ 6612	Sales						
52	^ 6613	Product Advertising						
53	6621	Call Completion Services						
54	6622	Number Services						
55	6623	Customer Services						
56	6711	Executive						
57	6712	Planning						
58	6721	Accounting and Finance						
59	6722	External Relations						
60	6723	Human Relations						
61	6724	Information Management						
62	6725	Legal						
63	6726	Procurement						
64	6727	Research and Development						
65	6728	Other General and Administrative						
66	6790	Provision for Uncollectible Notes Receivable						
67		<b>Totals</b>						

^ Subaccount of the account marked with a \*.

Total State Expense Matrix

Line No.	Accl. No. (a)	Description (b)	Salaries and Wages (c)	Benefits (d)	Rents (e)	Other Expenses (f)	Clearances (g)	Total (h)
1	*	Network Support Expense						
2	^	Motor Vehicle Expense						
3	^	Aircraft Expense						
4	^	Special Purpose Vehicles Expense						
5	^	Garage Work Equipment Expense						
6	^	Other Work Equipment Expense						
7	*	General Support Expense						
8	^	Land and Building Expense						
9	^	Furniture and Artworks Expense	N/A					
10	^	Office Equipment Expense						
11	^	General Purpose Computers Expense						
12	*	Central Office Switching Expense						
13	^	Analog Electronic Expense						
14	^	Digital Electronic Expense						
15	^	Electro-Mechanical Expense						
16		Operator Systems Expense						
17	*	Central Office Transmission Expense						
18	^	Radio Systems Expense						
19	^	Circuit Equipment Expense						
20	*	Information Origination/Termination Expense						
21	^	Station Apparatus Expense						
22	^	Large Private Branch Exchange Expense						
23	^	Public Telephone Terminal Equipment Exp.						
24	^	Other Terminal Equipment Expense						
25	*	Cable and Wire Facilities Expense						
26	^	Poles Expense						
27	^	Aerial Cable Expense						
28	^	Underground Cable Expense						
29	^	Buried Cable Expense						
30	^	Submarine Cable Expense						
31	^	Deep Sea Cable Expense						
32	^	Intrabuilding Network Cable Expense						
33	^	Aerial Wire Expense						
34		<b>Subtotals</b>						

^ Subaccount of the account marked with a \*

**Total State Expense Matrix**

Line No.	Acct. No. (a)	Description (b)	Salaries and Wages (c)	Benefits (d)	Rents (e)	Other Expenses (f)	Clearances (g)	Total (h)
35	^	Conduit Systems Expense						
36		Other Property Expenses						
37	*	Network Operations Expense						
38	^	Power Expense						
39	^	Network Administration Expense						
40	^	Testing Expense						
41	^	Plant Operations Expense						
42	^	Engineering Expense						
43		Access Expense						
44		Depreciation - Telecomm. Plant in Service						
45		Depreciation-Prop. for Future Telecom. Use						
46		Amortization Expense - Tangible						
47		Amortization Expense - Intangible						
48		Amortization - Other						
49	*	Marketing						
50	^	Product Management						
51	^	Sales						
52	^	Product Advertising						
53		Call Completion Services						
54		Number Services						
55		Customer Services						
56		Executive						
57		Planning						
58		Accounting and Finance						
59		External Relations						
60		Human Relations						
61		Information Management						
62		Legal						
63		Procurement						
64		Research and Development						
65		Other General and Administrative						
66		Provision for Uncollectible Notes Receivable						
67		<b>Totals</b>						

^ Subaccount of the account marked with a \*

**Pension Costs**

Year: 2008

1	Plan Name National Telephone Cooperative Retirement & Security			
2	Defined Benefit Plan? _____ YES _____	Defined Contribution Plan? _____		
3	Actuarial Cost Method? _____	IRS Code: _____		
4	Annual Contribution by Employer: ___ 104,221 ___	Is the Plan Over Funded? _____		
5				
	Item	Current Year	Last Year	% Change
6	<b>Change in Benefit Obligation</b>			
7	Benefit obligation at beginning of year			
8	Service cost			
9	Interest Cost			
10	Plan participants' contributions			
11	Amendments			
12	Actuarial Gain			
13	Acquisition			
14	Benefits paid			
15	Benefit obligation at end of year			
16	<b>Change in Plan Assets</b>			
17	Fair value of plan assets at beginning of year			
18	Actual return on plan assets			
19	Acquisition			
20	Employer contribution			
21	Plan participants' contributions			
22	Benefits paid			
23	Fair value of plan assets at end of year			
24	<b>Funded Status</b>			
25	Unrecognized net actuarial loss			
26	Unrecognized prior service cost			
27	Prepaid (accrued) benefit cost			
28				
29	<b>Weighted-average Assumptions as of Year End</b>			
30	Discount rate			
31	Expected return on plan assets			
32	Rate of compensation increase			
33				
34	<b>Components of Net Periodic Benefit Costs</b>			
35	Service cost			
36	Interest cost			
37	Expected return on plan assets			
38	Amortization of prior service cost			
39	Recognized net actuarial loss			
40	Net periodic benefit cost			
41				
42	<b>Montana Intrastate Costs:</b>			
43	Pension Costs			
44	Pension Costs Capitalized			
45	Accumulated Pension Asset (Liability) at Year End			
46	<b>Number of Company Employees:</b>			
47	Covered by the Plan			
48	Not Covered by the Plan			
49	Active			
50	Retired			
51	Deferred Vested Terminated			

**Other Post Employment Benefits (OPEBS)**

	Item	Current Year	Last Year	% Change
1	<b>Regulatory Treatment:</b>			
2	Commission authorized - most recent			
3	Docket number: _____			
4	Order number: _____			
5	Amount recovered through rates			
6	<b>Weighted-average Assumptions as of Year End</b>			
7	Discount rate			
8	Expected return on plan assets	N/A		N/A
9	Medical Cost Inflation Rate			
10	Actuarial Cost Method			
11	Rate of compensation increase			
12	<b>List each method used to fund OPEBs (ie: VEBA, 401(h)) and if tax advantaged:</b>			
13				
14				
15	<b>Describe any Changes to the Benefit Plan:</b>			
16				
17	<b>TOTAL COMPANY</b>			
18	<b>Change in Benefit Obligation</b>			
19	Benefit obligation at beginning of year			
20	Service cost			
21	Interest Cost			
22	Plan participants' contributions			
23	Amendments			
24	Actuarial Gain			
25	Acquisition			
26	Benefits paid			
27	Benefit obligation at end of year			
28	<b>Change in Plan Assets</b>			
29	Fair value of plan assets at beginning of year			
30	Actual return on plan assets			
31	Acquisition			
32	Employer contribution			
33	Plan participants' contributions			
34	Benefits paid			
35	Fair value of plan assets at end of year			
36	<b>Funded Status</b>			
37	Unrecognized net actuarial loss			
38	Unrecognized prior service cost			
39	Prepaid (accrued) benefit cost			
40	<b>Components of Net Periodic Benefit Costs</b>			
41	Service cost			
42	Interest cost			
43	Expected return on plan assets	#VALUE!		#VALUE!
44	Amortization of prior service cost			
45	Recognized net actuarial loss			
46	Net periodic benefit cost	#VALUE!		#VALUE!
47	<b>Accumulated Post Retirement Benefit Obligation</b>			
48	Amount Funded through VEBA			
49	Amount Funded through 401(h)			
50	Amount Funded through Other _____			
51	TOTAL			
52	Amount that was tax deductible - VEBA			
53	Amount that was tax deductible - 401(h)			
54	Amount that was tax deductible - Other _____			
55	TOTAL			

**Other Post Employment Benefits (OPEBS) Continued**

	Item	Current Year	Last Year	% Change
1	<b>Number of Company Employees:</b>			
2	Covered by the Plan			
3	Not Covered by the Plan			
4	Active			
5	Retired			
6	Spouses/Dependants covered by the Plan			
7	<b>Montana</b>			
8	<b>Change in Benefit Obligation</b>			
9	Benefit obligation at beginning of year			
10	Service cost			
11	Interest Cost			
12	Plan participants' contributions			
13	Amendments			
14	Actuarial Gain			
15	Acquisition			
16	Benefits paid			
17	Benefit obligation at end of year			
18	<b>Change in Plan Assets</b>			
19	Fair value of plan assets at beginning of year			
20	Actual return on plan assets			
21	Acquisition			
22	Employer contribution			
23	Plan participants' contributions			
24	Benefits paid			
25	Fair value of plan assets at end of year			
26	<b>Funded Status</b>			
27	Unrecognized net actuarial loss			
28	Unrecognized prior service cost			
29	Prepaid (accrued) benefit cost			
30	<b>Components of Net Periodic Benefit Costs</b>			
31	Service cost			
32	Interest cost			
33	Expected return on plan assets	#VALUE!		#VALUE!
34	Amortization of prior service cost			
35	Recognized net actuarial loss			
36	Net periodic benefit cost	#VALUE!		#VALUE!
37	<b>Accumulated Post Retirement Benefit Obligation</b>			
38	Amount Funded through VEBA			
39	Amount Funded through 401(h)			
40	Amount Funded through other _____			
41	TOTAL			
42	Amount that was tax deductible - VEBA			
43	Amount that was tax deductible - 401(h)			
44	Amount that was tax deductible - Other			
45	TOTAL			
46	<b>Montana Intrastate Costs:</b>			
47	Pension Costs			
48	Pension Costs Capitalized			
49	Accumulated Pension Asset (Liability) at Year End			
50	<b>Number of Montana Employees:</b>			
51	Covered by the Plan			
52	Not Covered by the Plan			
53	Active			
54	Retired			
55	Spouses/Dependants covered by the Plan			

**Payments for Services to Persons Other Than Employees**

Line No.	Name of Recipient (a)	Nature of Service (b)	Total Company Cost (c)	Total State Cost (d)	Intrastate Cost (e)
1	Not Applicable				
2					
3					
4					
5					
6					
7					
8					
9					
10					
11					
12					
13					
14					
15					
16					
17					
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28					
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31					
32					
33					
34					
35					
36					
37					
38					
39					
40					
41					
42					
43					
44					
45					
46					
47					
48					
49	<b>Total</b>				

**Subscriber Line Usage Data**

Line No.	Description (a)	This Year (b)	% of Total (c)	Last Year (d)
1	Toll Usage:			
2	Interstate, InterLATA	482240	14.79%	
3	Interstate, IntraLATA			
4	<b>Total Interstate Usage</b>	482240	14.79%	
5	Intrastate, InterLATA			
6	Intrastate, IntraLATA	2779443	85.21%	
7	<b>Total Intrastate Usage</b>	2779443	85.21%	
8	<b>Total Toll Usage</b>	3261683	100.00%	
9	Centrex			
10	Local			
11	<b>Total Minutes</b>	3261683	100.00%	



**Central Office and Access Line Statistics**

Year: 2008

Line No.	Wire Center (a)	Type of Office (b)	Residential (c)	ISDN (d)	ADSL (e)	Lifeline Customers (f)	Residential LMS Customers (g)	Single Line Business (h)	Multi-Line Business (i)	Customer Owned Coin (j)	Company Owned Coin (k)	Other (l)	% of Lines w/ T. Tone (m)	Total Access Lines (n)
1	Divide	Digital	80			1		14			1			95
2	Grant	Digital	75			1		14			1			90
3	Jackson	Digital	264			1		45			2			311
4	Wisdom	Digital	169					61	15		1			246
5	Wise River	Digital	233			1		27	12		1			273
6														
7														
8														
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29														
30														
31														
32														
33	<b>Total</b>		821			4		161	27		6			1015

NOTE: Additional blank schedules are being provided for your convenience.

Central Office and Switch Information

Year: 2008

Line No.	Wire Center (a)	Office Configuration (Host, Remote, Stand alone) (b)	Type of Switch (c)	Switch Vendor/Manufacturer (d)	Switch Model No. (e)	Switch Line Capacity (f)	Year Deployed (g)
1	406-267	Remote	Digital	Nortel	DMS-10	512	1990
2	406-832	Remote	Digital	Nortel	DMS-10	512	1983
3	406-689-S	Remote	Digital	Nortel	DMS-10	512	1983
4	406-689	Host	Digital	Nortel	DMS-10	640	1983
5	406-834-J	Remote	Digital	Nortel	DMS-10	512	1983
6	406-834-T	Remote	Digital	Nortel	DMS-10	512	1983
7	406-681	Remote	Digital	Nortel	DMS-10	512	1983
8							
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48							

**Construction Budget - Montana**

Year:

Line No.	Description (a)	(b)
1	<b>Central Office Assets:</b>	
2		
3		
4		
5		
6		
7		
8		
9		
10		
11		
12		
13		
14		
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16		
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22		
23		
24		
25		
26		
27	Total Switching and Central Office Projects over \$500,000	
28	Miscellaneous Central Office Projects not over \$500,000	
29	<b>Total Central Office Budget (Total of Line 27 &amp; Line 28)</b>	
30	<b>Other Projects over \$500,000:</b>	
31		
32	Outside Plant Construction & Engineering	750000
33	Transport Engineering/ Subscriber Electronics	350000
34		
35		
36		
37		
38		
39		
40		
41	Total Other Projects over \$500,000	1100000
42	Miscellaneous projects not over \$500,000	100000
43	<b>Total Construction Budget (Total of Lines 29, 41 &amp; 42)</b>	1200000

### Montana Total State Construction Expenditures

Line No.	FCC Part 32 Account No. (a)	Description (b)	This Year (c)	Last Year (d)	Percent Change (e)
1	2110	General Support Assets	44399		
2	2210	Central Office Assets	72139		
3	2220	Operator Systems	0		
4	2230	Central Office Transmission	272147		
5	2310	Information/Termination Assets	0		
6	2410	Cable and Wire Facilities Assets	926067		
7	2680	Amortizable Tangible Assets	0		
8	2690	Intangibles	0		
9		<b>Total Construction Expenditures</b>	<b>1314752</b>		

Montana Employee Counts

Year: 2008

Line No.	Category (a)	Beginning of Year (b)	End of Year (c)
1	Executive	2	2
2	Office	3	3
3	Outside Plant-COE	2	3
4			
5			
6			
7			
8			
9			
10			
11			
12			
13			
14			
15			
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39			
40			
41			
42			
43	<b>Totals (Sum of Lines 1 through 42)</b>	7	8

**Compensation of Top 10 Montana Based Employees**

Year: 2008

Line No.	Name/Title (a)	Base Salary (b)	Bonuses (c)	Other Compensation (d)	Total Compensation (e)	Total Compensation Last Year (f)	% Increase Total Compensation (g)
1							
2							
3	Filed under Separate Cover This information is proprietary and is filed under Protective Order						
4							
5							
6							
7							
8							
9							
10							
11	<b>Totals (Sum L.1 to L.10)</b>						

**Compensation of Top 5 Corporate Employees - SEC Information**

Line No.	Name/Title (a)	Base Salary (b)	Bonuses (c)	Other Compensation (d)	Total Compensation (e)	Total Compensation Last Year (f)	% Increase Total Compensation (g)
1							
2	N/A						
3							
4							
5							
6	<b>Totals (Sum L.1 to L.5)</b>						

Montana Composite Statistics

Year: 2008

Line No.	Account No.	Description (a)	Amount (b)
1		<b>Plant (Intrastate Only) (000 Omitted)</b>	
2	2001	Plant in Service	N/A
3	2003 - 2004	Construction Work in Progress	
4	2005	Plant Acquisition Adjustments	
5	2002	Plant Held for Future Use	
6	1220	Materials & Supplies	
7		(Less):	
8	3100 - 3400	Depreciation & Amortization Reserves	
9	4360.2	Contributions in Aid of Construction	
10		<b>NET BOOK COSTS</b>	
11		<b>Revenues &amp; Expenses (Intrastate Only) (000 Omitted)</b>	
12	5000 - 5300	Operating Revenues	
13	6560	Depreciation & Amortization Expenses	
14		Federal & State Income Taxes	
15		Other Taxes	
16		Other Operating Expenses	
17		TOTAL Operating Expenses	
18		Net Operating Income	
19		Other Income	
20		Other Deductions	
21		<b>NET INCOME</b>	
22		<b>Access Lines in Service (Intrastate Only)</b>	
23		Residential Access Lines	
24		Business Access Lines	
25		PBX Access Lines	
26		Other Access Lines	
27		<b>Total Number of Access Lines</b>	
28		<b>Average Number of Calls Per Access Line</b>	
29		Local Calls	
30		Toll Calls (Intra- or Interstate)	
31		<b>Total Number of Calls Per Access Line</b> <b>(Total of Line 29 &amp; Line 30 divided by Line 27)</b>	
32		<b>Other Statistics (Intrastate Only)</b>	
33		Average Residential Monthly Bill	
34		Gross Plant Investment per Access Line	



**Depreciation - Montana Intrastate Regulated**

Year: 2008

Line No.	Acct No. (a)	Description (b)	Composite Rate % (c)	Total Expense \$ (d)
1	2112	Motor Vehicles	33.0%	
2	2114	Special Purpose Vehicles		
3	2115	Garage Work Equipment		
4	2116	Other work Equipment	13.4%	
5	2121	Buildings	4.2%	26,914
6	2122	Furniture		
7	2123.1	Office Support Equipment	11.7%	3,061
8	2123.2	Company Communications Equipment	9.3%	
9	2124	General Purpose Computers	20.0%	6,451
10	2211	Analog Electronic Switching Equipment		
11	2212	Digital Electronic Switching Equipment	10.0%	279,366
12	2215	Step By Step Switching Equipment		
13	2215	Crossbar Switching Equipment		
14	2220	Operator System		
15	2231	Radio Systems		
16	2232	Circuit DDS		
17	2232	Circuit Digital		
18	2232	Circuit Analog		
19	2351	Public Telephone Terminating Equipment		
20	2362	Other Terminal Equipment		
21	2411	Poles		
22	2421	Aerial Cable Metallic		
23	2421	Aerial Cable Nonmetallic		
24	2422	Underground Cable Metallic		
25	2422	Underground Cable Nonmetallic		
26	2423	Buried Cable Metallic	5.0%	205,937
27	2423	Buried Cable Nonmetallic	5.0%	154,483
28	2424	Submarine Cable Metallic		
29	2424	Submarine Cable Nonmetallic		
30	2426	Intrabuilding Network Cable Metallic		
31	2426	Intrabuilding Network Cable Nonmetallic		
32	2431	Aerial Wire	5.0%	1,669
33	2441	Conduit Systems		
34				
35		<b>COMPOSITE TOTAL</b>		677,881
36	<p><b>Please list the Montana Public Service Commission Docket Order No. approving these depreciation rates</b></p> <p>Docket Number _____ Order Number _____</p>			
37				
38				
39				
40				

**Amortization - Montana Intrastate Regulated**

Year: 2008

Line No.	Acct No. (a)	Description (b)	Composite Rate % (c)	Total Expense \$ (d)
1				
2				
3				
4				
5		N/A		
6				
7				
8				
9				
10				
11				
12				
13				
14				
15				
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24				
25				
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29				
30				
31				
32				
33				
34				
35		<b>COMPOSITE TOTAL</b>		
36	<b>Please list the Montana Public Service Commission Docket Order No. approving these amortization rates</b>			
37				
38				
39	Docket Number _____ Order Number _____			
40				

**Montana Regulatory Capital Structure & Costs**

Year: 2008

Line No.	Description (a)	% Cap. Str. (b)	% Cost Rate (c)	Weighted Cost (d)
<b>Commission Accepted - Most Recent</b>				
1	Docket Number _____			
2	Order Number _____			
3				
4	Common Equity			
5	Preferred Stock			
6	Long Term Debt			
7	Other			
8	<b>Total</b>			
<b>Actual at Year End</b>				
12	Common Equity			
13	Preferred Stock			
14	Long Term Debt			
15	Other			
16	<b>Total</b>			

**Network Access - Charges and Revenues**

Year: 2008

Line No.	Description (a)	Access Charges Paid (b)	Access Revenues Received (c)
1	Montana - Total State		463222
2			
3	Montana - Intrastate		463222
4			
5	Montana - Intrastate Regulated		463222
6			
7			
8			
9			
10			
11			
12			
13			

Affiliate Transactions - Products & Services Provided to Utility Year: 2008

Line No.	Affiliate Name (a)	Products & Services (b)	Method to Determine Price (c)	Charges to Utility to Utility (d)	% Total Affil. Revenues (e)	Charges to MT Utility (f)	
1	National Information Systems	Computer Service Bureau- Accounting support Customer Billing, Plant, Software Support CABS Billing	Varies			98,989	
2							
3							
4							
5							
6							
7							
8	GWNW, Inc.	Management Consultantx Cost Studies Seperations	Hourly Rate			90,386	
9							
10							
11							
12							
13	Moss-Adams	Audit, Management Consultants	Hourly rate			17,815	
14							
15							
16							
17							
18							
19							
20							
21							
22							
23							
24							
25							
26							
27							
28							
29							
30	<b>TOTAL</b>						\$207,190

**Affiliate Transactions - Products & Services Provided by Utility**

Year: 2008

Line No.	Affiliate Name (a)	Products & Services (b)	Method to Determine Price (c)	Charges to Affiliate (d)	% Total Affil. Revenues (e)	Charges to MT Utility (f)
1						
2						
3						
4						
5						
6						
7						
8						
9						
10						
11						
12						
13						
14						
15						
16						
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24						
25						
26						
27						
28						
29						
<b>30</b>	<b>TOTAL</b>					

**Montana Intrastate Regulated Earned Rate of Return**

Year: 2008

Line No.	Description Rate Base (a)	This Year (b)	Last Year (c)	Percent Change (d)
1				
2	2001 Plant in Service			
3	2002 Prop. Held for Future Telecommunications Use			
4	3100-3200 (Less) Accumulated Depreciation			
5	<b>Plant in Service</b>			
6				
7	<b>Additions</b>			
8	1220 Materials & Supplies			
9	1280 Prepayments			
10	Other Additions			
11	<b>TOTAL Additions</b>			
12				
13	<b>Deductions</b>			
14	4100 Current Deferred Operating Income Taxes			
15	4320 Unamortized Operating Investment Tax Credits			
16	4340 Noncurrent Deferred Operating Income Taxes			
17	Customer Advances for Construction			
18	Other Deductions			
19	<b>TOTAL Deductions</b>			
20	<b>TOTAL Rate Base</b>			
21				
22	<b>Net Earnings</b>			
23				
24	<b>Rate of Return on Average Rate Base</b>			
25				
26	<b>Rate of Return on Average Equity</b>			
27				
28	Major Normalizing Adjustments & Commission			
29	Rate-making adjustments to Utility Operations			
30				
31				
32				
33				
34				
35				
36				
37				
38				
39				
40				
41				
42				
43	<b>Adjusted Rate of Return on Average Rate Base</b>			
44				
45	<b>Adjusted Rate of Return on Average Equity</b>			

**Other Taxes Paid**

Year: 2008

Line No.	Description (a)	Last Year (b)	This Year (c)
1	Montana Telephone Company License Tax		572
2	Montana Public Service Commission Tax		2077
3	Montana Consumer Counsel Tax		938
4	911 Emergency Telephone Fee		
5	Montana Telecommunications Access Service (TDD)		
6	Montana Corporate License Tax		
7	Personal Property Tax		
8	Real Property Tax		59772
9			
10			
11			
12	<b>Total</b>		63359

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**Universal Service Funds Received**

Year: 2008

Line No.	Description (a)	Last Year (b)	This Year (c)
13	Funds received from Montana Sources		
14	Funds received from Federal Sources		498063
15			
16			
17			
18			
19			
20			
21			
22			
23			
24	<b>Total</b>		498063

**SOUTHERN MONTANA TELEPHONE COMPANY**

Financial Statements

Years Ended December 31, 2008 and 2007



# **SOUTHERN MONTANA TELEPHONE COMPANY**

## **Financial Statements**

Years Ended December 31, 2008 and 2007

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## INDEPENDENT AUDITORS' REPORT

To the Board of Directors  
Southern Montana Telephone Company  
Wisdom, Montana

We have audited the accompanying balance sheets of Southern Montana Telephone Company (the Company) as of December 31, 2008, and the related statements of income, changes in stockholders' equity, and cash flows for the year 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 audit. The financial statements of Southern Montana Telephone Company, as of December 31, 2007, were audited by other auditors, whose report dated March 18, 2008, expressed an unqualified opinion on those statements.

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 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 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 audit provides 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 Southern Montana Telephone Company as of December 31, 2008, and the results of their operations and their cash flows for the year 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 our report dated April 22, 2009 on our consideration of Southern Montana Telephone Company's internal control over financial reporting and our tests of its compliance with laws, regulations, contracts, and grants. 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 the internal control over financial reporting or on compliance. That reporting 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 audit.

**AKT LLP**

Salem, Oregon  
April 22, 2009

# SOUTHERN MONTANA TELEPHONE COMPANY

## Balance Sheets

December 31, 2008 and 2007

<b>ASSETS</b>	<u>2008</u>	<u>2007</u>
Current Assets:		
Cash and cash equivalents	\$ 1,806,514	\$ 1,889,500
Marketable securities	-	40,000
Accounts receivable, less allowance for doubtful accounts of \$16,057 (\$20,266 in 2007)	283,129	363,755
Materials and supplies	63,625	63,538
Prepaid expenses	<u>28,048</u>	<u>4,900</u>
Total Current Assets	<u>2,181,316</u>	<u>2,361,693</u>
Other investments	352,501	351,067
Property, Plant, and Equipment:		
In-service	12,475,685	11,180,524
Under construction	<u>2,013,665</u>	<u>367,366</u>
	14,489,350	11,547,890
Less accumulated depreciation	<u>6,642,614</u>	<u>5,971,996</u>
Property, Plant, and Equipment, net	<u>7,846,736</u>	<u>5,575,894</u>
	<u>\$ 10,380,553</u>	<u>\$ 8,288,654</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current Liabilities:		
Current portion of long-term debt	\$ 282,221	\$ 304,936
Accounts payable	68,662	129,539
Advance billing and customer deposits	16,076	27,663
Accrued expenses	<u>388,253</u>	<u>192,833</u>
Total Current Liabilities	<u>755,212</u>	<u>654,971</u>
Long-Term Debt	<u>5,945,186</u>	<u>3,738,976</u>
Stockholders' Equity:		
Common stock, \$10 par value, 2,703 shares authorized and 610 shares issued and outstanding	6,100	6,100
Paid-in capital	3,290	3,290
Retained earnings	<u>3,670,765</u>	<u>3,885,317</u>
Total Stockholders' Equity	<u>3,680,155</u>	<u>3,894,707</u>
	<u>\$ 10,380,553</u>	<u>\$ 8,288,654</u>

See accompanying notes to consolidated financial statements.

# SOUTHERN MONTANA TELEPHONE COMPANY

## Statements of Income

Years Ended December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Operating Revenues:		
Local network	\$ 178,843	\$ 186,274
Interstate access	1,919,946	1,736,981
Intrastate access	470,949	405,697
Miscellaneous	<u>5,366</u>	<u>3,772</u>
Total Operating Revenues	<u>2,575,104</u>	<u>2,332,724</u>
Operating Expenses:		
Plant specific operations	407,169	483,618
Plant nonspecific operations	180,703	299,760
Customer	67,635	53,034
Corporate	874,999	586,597
Depreciation and amortization	675,903	597,798
Other operating taxes	63,359	46,986
Nonregulated, net	<u>135,554</u>	<u>71,649</u>
Total Operating Expenses	<u>2,405,322</u>	<u>2,139,442</u>
Operating Income	169,782	193,282
Other Income (Expense):		
Other Income (Expense)	(93,827)	97,410
Allowance for funds used during construction	<u>39,674</u>	<u>15,248</u>
Total Other Income (Expense)	<u>(54,153)</u>	<u>112,658</u>
Income Available for Fixed Charges	115,629	305,940
Fixed Charges - Interest on Long-Term Debt	<u>189,695</u>	<u>91,589</u>
Net Income (Loss)	<u>\$ (74,066)</u>	<u>\$ 214,351</u>

**SOUTHERN MONTANA TELEPHONE COMPANY**

**Statements of Changes in Stockholders' Equity**

Years Ended December 31, 2008 and 2007

	Capital Stock		Paid-in Capital	Retained Earnings	Accumulated Other	Total
	Shares Issued	Amount			Comprehensive Income	
Balance, December 31, 2006	610	\$ 6,100	\$ 3,290	\$ 3,810,506	\$ (10,605)	\$ 3,809,291
Change in unrealized loss on available for sale securities	-	-	-	-	26,100	26,100
Reclassification adjustment	-	-	-	-	(15,495)	(15,495)
Distributions	-	-	-	(139,540)	-	(139,540)
Net income	-	-	-	214,351	-	214,351
Balance, December 31, 2007	610	6,100	3,290	3,885,317	-	3,894,707
Distributions	-	-	-	(140,486)	-	(140,486)
Net loss	-	-	-	(74,066)	-	(74,066)
Balance, December 31, 2008	<u>610</u>	<u>\$ 6,100</u>	<u>\$ 3,290</u>	<u>3,670,765</u>	<u>\$ -</u>	<u>\$ 3,680,155</u>

**SOUTHERN MONTANA TELEPHONE COMPANY****Statements of Cash Flows**

Years Ended December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Cash Flows from Operating Activities:		
Net income (loss)	\$ (74,066)	\$ 214,351
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	675,903	597,798
Patronage capital credits, noncash	-	(16,668)
Realized (gain) loss on sale of marketable securities	-	(15,495)
Changes in assets and liabilities:		
Accounts receivable	80,626	28,254
Materials and supplies	(87)	(7,111)
Prepaid expenses	(23,148)	1,792
Accounts payable	(60,877)	(150,556)
Advance billing and customer deposits	(11,587)	(9,495)
Accrued expenses	195,420	(5,299)
Net Cash Provided by Operating Activities	<u>782,184</u>	<u>637,571</u>
Cash Flows from Investing Activities:		
Capital expenditures	(2,946,745)	(2,733,712)
Purchase of other investments	-	(1,191,482)
Proceeds from sale of marketable securities and investments	38,566	1,441,497
Net Cash Used by Investing Activities	<u>(2,908,179)</u>	<u>(2,483,697)</u>
Cash Flows from Financing Activities:		
Proceeds from long-term debt	2,413,061	3,380,129
Payments on long-term debt	(229,566)	(1,118,880)
Equity distributions	(140,486)	(139,540)
Net Cash Provided by Financing Activities	<u>2,043,009</u>	<u>2,121,709</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(82,986)	275,583
Cash and Cash Equivalents, beginning	<u>1,889,500</u>	<u>1,613,917</u>
Cash and Cash Equivalents, ending	\$ <u>1,806,514</u>	\$ <u>1,889,500</u>
Cash Paid During the Year for Interest, net of amount capitalized	\$ <u>150,021</u>	\$ <u>76,341</u>

See accompanying notes to consolidated financial statements.

## **SOUTHERN MONTANA TELEPHONE COMPANY**

### **Notes to Financial Statements**

Years Ended December 31, 2008 and 2007

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#### **Note 1 - Organization and Summary of Significant Accounting Policies**

##### Organization

Southern Montana Telephone Company (the Company) is a local exchange carrier (LEC) providing local telephone service, Internet access, and long-distance telecommunications services. The Company serves commercial and residential customers in the southwestern Montana exchanges of Divide, Grant, Jackson, Wisdom, and Wise River.

##### Regulation

The Company is subject to limited regulation by the Public Utility Commission of Montana (PUC). The Company maintains its accounting records in accordance with the Uniform System of Accounts, as prescribed by the Federal Communications Commission (FCC), and adopted by the PUC. Regulatory actions currently pending, as well as future regulations, could have a significant impact on the Company's operations and financial condition.

##### Cash and Cash Equivalents

The Company considers cash investments with an original maturity of 3 months or less to be cash equivalents. The Company maintains its cash in bank deposit accounts that, at times, may exceed federally insured limits. Section 136 of the Emergency Economic Stabilization Act of 2008 temporarily increased FDIC deposit insurance limits from \$100,000 to \$250,000 until December 31, 2009. Further, the Company's bank participates in the FDIC's Temporary Liquidity Guarantee Program, whereby all non-interest bearing accounts are fully insured. The Company also has cash equivalents in money market funds through brokerage accounts that are fully insured through the U.S Treasury's Temporary Guarantee Program for Money Market Funds. As such, there are no uninsured balances at December 31, 2008.

##### Accounts Receivable

The Company extends credit to its customers. Receivables are written off when the Company determines an account is uncollectible. Past due status is determined based on how recently the payment has been received. Credit risk associated with receivables is periodically reviewed by management and, if required, an allowance for doubtful accounts is established.

##### Estimates

The Company uses estimates and assumptions in preparing financial statements in accordance with accounting principles generally accepted in the United States of America. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses.

##### Income Taxes

The Company is designated as an S corporation under the Internal Revenue Code. As an S corporation, earnings and losses are included in the income tax returns of the stockholders and taxed at the stockholder level. Accordingly, the Company does not incur additional income tax obligations, and financial statements do not include a provision for income taxes.

##### Materials and Supplies

Materials and supplies are stated at the lower of cost or market. Cost is determined principally by the average cost method.

##### Property, Plant, and Equipment

Telecommunications plant in service and under construction is stated at cost, including estimated overhead expense. Depreciation is calculated on a straight-line basis over the estimated life of the classes of buildings and equipment in accordance with rates consistent with industry standards. Depreciation rates range from 4.2% to 33.3%. Costs of plant retired are eliminated from telecommunications plant accounts and such costs plus removal expenses, less salvage, are charged to depreciation.

## SOUTHERN MONTANA TELEPHONE COMPANY

### Notes to Financial Statements

Years Ended December 31, 2008 and 2007

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#### Note 1 - Organization and Summary of Significant Accounting Policies, continued

##### Property, Plant, and Equipment, continued

The Company follows the policy of capitalizing interest as a component of the cost of property, plant, and equipment constructed for its own use. In 2008, total interest incurred was \$189,695 (\$91,589 in 2007), \$39,674 of which was capitalized in 2008 (\$15,248 in 2007).

##### Nonregulated Services

The Company accounts for its nonregulated activities as follows:

Nonregulated activities involving the joint use of regulated assets are accounted for within the prescribed regulated system of accounts for telephone company operations. These activities include directory services, long distance services, and other income items incidental to the provision of regulated telephone services.

Nonregulated activities not involving the joint use of regulated assets are accounted for separately from regulated activities. Operating revenues and the related expenses are separately presented as nonregulated revenues and expenses. These activities include Internet and payphone services.

##### Comprehensive Income

The Company follows SFAS Statement No. 130, Reporting Comprehensive Income. The purpose of reporting comprehensive income is to report all changes in equity of an enterprise that result from recognized transactions and other economic events of the period other than transactions with owners in their capacity as owners.

##### Network Access Revenues

Network access revenue for intralata and interlata toll service is received under a system of access charges. Access charges represent a methodology by which local telephone companies, including the Company, charge the long distance carrier for access and interconnection to local facilities. The Company follows an access tariff filed with the PUC and FCC for these charges.

When network access revenues have been received pursuant to the settlement and access agreements above, they are divided into traffic sensitive, nontraffic sensitive, and billing and collecting portions. The revenues are then either placed into a common pooling arrangement with other exchange carriers for redistribution or kept by the Company. The redistributions are made according to formulas established by the governing boards of the pools and are generally based upon expenses incurred and investment maintained. The Company participates in pooling arrangements with the National Exchange Carrier Association (NECA).

Settlement, access, and pool distribution revenues are recorded when the amounts become determinable. Related expenses are recorded when incurred. Subsequent true-ups and retroactive adjustments, which are generally allowed for a period of 24 months after the close of the related calendar years (NECA only), are recorded in the year in which such adjustments become determinable, based upon studies by an outside consultant.

In addition to recoveries from NECA, the Company also receives revenues from the Universal Service High Cost Loop Fund administered by the Universal Service Administration Company (USAC). Amounts received from USAC are the result of having costs in excess of the national average as determined by the FCC and are included in network access revenues in the accompanying financial statements. In 2008, the Company received \$442,872 from the USAC High Cost Loop Fund (\$284,658 in 2007).

The ability of NECA and USAC to provide these revenues to the Company and similar organizations is dependent upon regulatory and legislative rules which provide for the continuance of rate of return regulation and universal service support. Any regulatory or legislative change, which reduces the rate of return or the universal service support, may have a material impact on the Company.



## SOUTHERN MONTANA TELEPHONE COMPANY

### Notes to Financial Statements

Years Ended December 31, 2008 and 2007

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#### Note 2 - Property, Plant, and Equipment

Listed below are the major classes of property, plant, and equipment in service:

	<u>2008</u>	<u>2007</u>
Telecommunications:		
Land and support	\$ 1,522,290	\$ 1,498,135
Central office	3,114,087	2,768,925
Cable and wire facilities	<u>7,839,308</u>	<u>6,913,464</u>
Total Telecommunications:	\$ <u>12,475,685</u>	\$ <u>11,180,524</u>

#### Note 3 - Investments in Debt and Marketable Equity Securities

SFAS Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities, requires classifying investments in marketable securities into one or more of three categories: held to maturity, available for sale, or trading, based upon the Company's ability and intent to hold the investment to maturity.

At December 31, 2007, the Company had \$40,000 of debt securities categorized as held to maturity and reported at cost, which approximated fair value. In 2008, the Company had proceeds from the sale of the debt securities of \$40,000.

#### Note 4 - Investments in Nonaffiliates

Investments in nonaffiliates consist of the following assets at December 31:

	<u>2008</u>	<u>2007</u>
Vision Net, Inc.	\$ 279,861	\$ 279,861
Other investments	32,501	30,859
RTFC	2,802	3,010
Artwork	31,547	31,547
Other Office Décor	<u>5,790</u>	<u>5,790</u>
	\$ <u>352,501</u>	\$ <u>351,067</u>

Vision Net, Inc. provides advanced voice, data, and video services and is owned by Montana's independent telephone companies allowing them to interconnect a digital fiber network serving urban and rural communities throughout the state. The investment is maintained on the cost method of accounting.

#### Note 5 - Long-Term Debt

Long-term debt consists of the following:

	<u>2008</u>	<u>2007</u>
2.00% notes payable to the Rural Utilities Service, payable in monthly installments of \$42,406, principal and interest, collateralized by substantially all real and personal property, due 2016 through 2023.	\$ 1,190,468	\$ 1,338,732
4.634 to 4.88% mortgage notes payable to the Rural Utilities Service, payable in monthly installments of \$9,899, principal and interest, collateralized by substantially all real and personal property, due in 2026.	2,480,134	2,480,129
2.692-4.58% notes payable to Rural Utilities Service, interest only through June 2010, then payable in monthly installments of \$14,690, collateralized by substantially all real and personal property, due in 2026.	<u>2,413,061</u>	<u>-</u>
Carried forward	\$ <u>6,083,663</u>	\$ <u>3,818,861</u>

## SOUTHERN MONTANA TELEPHONE COMPANY

### Notes to Financial Statements

Years Ended December 31, 2008 and 2007

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#### Note 5 - Long-Term Debt, continued

	<u>2008</u>	<u>2007</u>
Brought forward	\$ 6,083,663	\$ 3,818,861
7.50% note payable to Michelle Helming, a former stockholder and related party of the Company, payable in monthly installments of \$7,893.60, principal and interest, due in July of 2010.	<u>143,744</u>	<u>225,051</u>
	6,227,407	4,043,912
Less current portion	<u>282,221</u>	<u>304,936</u>
	<u>\$ 5,945,186</u>	<u>\$ 3,738,976</u>

The terms of the debt agreements contain restrictions on the declaration or payment of cash dividends, redemption of capital stock, and the maintenance of a minimum times interest earned ratio. Management believes the Company to be in compliance with these covenants at December 31, 2008.

At December 31, 2008, the Company had \$6,341,810 in unadvanced authorized loan funds from the Rural Utilities Services (\$8,754,871 at December 31, 2007).

Future maturities of long-term debt are as follows:

2009	\$ 282,221
2010	335,397
2011	373,565
2012	386,547
2013	400,045
Thereafter	4,449,632

#### Note 6 - Retirement Plans

The Company participates in a qualified multi-employer, non contributory, defined benefit plan (the Plan) administered by the Retirement and Security Program of the National Telecommunications Cooperative Association (NTCA), which covers all full-time eligible employees, and contributes 12% of each eligible employee's annual salary to the Plan. Pension costs include current service costs that are accrued and funded on a current basis. Total pension plan charges, including amounts charged to construction, were \$80,004 in 2008 (\$76,888 in 2007).

The Company also participates in a contributory, multi-employer, defined contribution plan administered by NTCA, which covers all full-time employees. Employees are required to contribute a minimum of 2% of their annual salary to participate in the plan. Employer contributions are 5% of eligible salaries paid. Employer contributions to the plan were \$24,217 in 2008 (\$27,757 in 2007).

#### Note 7 - Workers' Compensation

The Company is a member of the Montana Electric and Telephone Systems Self-Insured Workers' Compensation Pool (the Pool). The Pool covers potential liability for workers' compensation and occupational disease to employees and dependents of deceased employees of all members in the Pool. The Company is jointly and severally liable with the other members for the full amount of all known and unknown claims.

## SOUTHERN MONTANA TELEPHONE COMPANY

### Notes to Financial Statements

Years Ended December 31, 2008 and 2007

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#### Note 8 - Related Party Transactions

The Company leases its office building from Robert G. Helming, stockholder, officer, and director of the Company. The lease calls for monthly payments of \$2,200 through December 31, 2011. Subsequent to December 31, 2008 the Company entered into a new agreement with Robert Helming, which calls for monthly payments of \$3,100 effective April 2009.

Following is a summary of minimum rental payments under the lease for the years subsequent to December 31, 2008:

2009	\$ 35,400
2010	37,200
2011	37,200
2012	37,200
2013	37,200

Total rental expense under the lease listed above was approximately \$26,400 for the years ended December 31, 2008 and 2007.

#### Note 9 - Commitments

The Company has executed several contracts for construction projects. The amounts unpaid against these commitments at December 31, 2008 were \$282,277 (\$360,660 at December 31, 2007).

#### Note 10 - Reclassifications

Certain accounts in the 2007 financial statements have been reclassified to conform to the presentation in the 2008 financial statements. Such reclassifications have no effect on net income.