

PUBLIC SERVICE COMMISSION  
ANNUAL REPORT BRANCH  
APR 2 2012  
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**BRANDENBURG TELEPHONE COMPANY**

**FINANCIAL STATEMENTS**

**DECEMBER 31, 2011 AND 2010**

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William A. Talley  
Jon D. Chesser  
Bob E. Wientjes

Kentucky Offices:  
Louisville  
Brandenburg  
Bardstown

**INDEPENDENT AUDITORS' REPORT**

To the Board of Directors  
Brandenburg Telephone Company  
Brandenburg, Kentucky

We have audited the accompanying balance sheets of Brandenburg Telephone Company as of December 31, 2011 and 2010, and the related statements of income, changes in stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of Brandenburg Telephone Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Brandenburg Telephone Company as of December 31, 2011 and 2010, and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 20, 2012, on our consideration of Brandenburg Telephone Company's internal control over financial reporting and 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 the 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 is important for assessing the results of our audit.

*Richardson, Pennington & Skinner, PSC.*

Louisville, Kentucky  
March 20, 2012

**BRANDENBURG TELEPHONE COMPANY**  
**BALANCE SHEETS**  
**DECEMBER 31, 2011 AND 2010**

<u>ASSETS</u>	<u>2011</u>	<u>2010</u>
Current Assets:		
Cash and cash equivalents	\$ 15,189,023	\$ 14,045,227
Accounts receivable	2,199,709	2,134,298
Income tax receivable	825,209	1,213,771
Due from affiliate	12,655,607	11,330,849
Materials and supplies, at average cost - based on the lower of cost or market	1,211,962	1,375,857
Prepaid insurance	28,820	82,130
	<hr/>	<hr/>
Total Current Assets	32,110,330	30,182,132
Non-Current Assets:		
Portfolio investments, available for sale	2,436,542	2,412,754
Investment in nonregulated	698,265	429,294
Deferred income taxes (Note J)	8,229,224	8,444,585
	<hr/>	<hr/>
Total Non-Current Assets	11,364,031	11,286,633
Telephone Plant, at original cost (Note A):		
Telephone plant under construction	87,828	80,496
Telecommunications plant (Note I)	73,772,793	72,473,831
	<hr/>	<hr/>
	73,860,621	72,554,327
Less: Accumulated Depreciation	73,401,747	72,473,826
	<hr/>	<hr/>
Total Telephone Plant	458,874	80,501
	<hr/>	<hr/>
<b>TOTAL ASSETS</b>	<b><u>\$ 43,933,235</u></b>	<b><u>\$ 41,549,266</u></b>

See independent auditors' report.  
See notes to financial statements.

**BRANDENBURG TELEPHONE COMPANY**  
**BALANCE SHEETS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

LIABILITIES AND STOCKHOLDERS' EQUITY

<u>LIABILITIES</u>	<u>2011</u>	<u>2010</u>
Current Liabilities:		
Accounts payable	\$ 780,714	\$ 527,988
Customer deposits	24,431	29,121
Other current and accrued liabilities	<u>10,408,578</u>	<u>4,987,141</u>
 Total Current Liabilities	 <u>11,213,723</u>	 <u>5,544,250</u>
 TOTAL LIABILITIES	 11,213,723	 5,544,250
 <u>STOCKHOLDERS' EQUITY</u>		
Common stock, \$50 par value; authorized shares, 100,000; issued and outstanding shares, 100,000.	5,000,000	5,000,000
Retained Earnings	32,610,437	32,843,324
Accumulated other comprehensive income		
Unrealized gains (losses) on securities	14,035	8,279
Change in Pension Accrual	<u>(4,904,960)</u>	<u>(1,846,587)</u>
 TOTAL STOCKHOLDERS' EQUITY	 <u>32,719,512</u>	 <u>36,005,016</u>
 <b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY</b>	 <b><u>\$ 43,933,235</u></b>	 <b><u>\$ 41,549,266</u></b>

See independent auditors' report.  
See notes to financial statements.

**BRANDENBURG TELEPHONE COMPANY**  
**STATEMENTS OF INCOME**  
**FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
Operating Revenues:		
Local network service	\$ 3,669,656	\$ 3,999,851
Network access service	11,433,869	10,077,586
Long distance network service	709,856	883,419
Miscellaneous revenue	<u>1,526,890</u>	<u>1,909,531</u>
Total Operating Revenues	17,340,271	16,870,387
Operating Expenses:		
Plant specific operations expense	3,198,340	2,951,483
Plant non-specific operations	1,112,191	1,065,371
Depreciation	1,194,189	4,131,006
Customer operation expense	2,042,549	2,212,769
Corporate operation expense	3,069,571	3,509,957
Other taxes	<u>414,282</u>	<u>312,489</u>
Total Operating Expenses	11,031,122	14,183,075
Operating Income	6,309,149	2,687,312
Other Income (Expense)		
Interest income	36,899	10,677
Interest expense	(1,265)	(1,583)
Other income	<u>302,049</u>	<u>224,744</u>
Total Other Income (Expenses)	<u>337,683</u>	<u>233,838</u>
Income Before Nonregulated Income	6,646,832	2,921,150
Nonregulated Income	<u>2,102,750</u>	<u>2,098,568</u>
Net Income Before Income Taxes	8,749,582	5,019,718
Income Taxes	<u>3,982,469</u>	<u>1,427,846</u>
Net Income	<u>\$ 4,767,113</u>	<u>\$ 3,591,872</u>

See independent auditors' report.  
See notes to financial statements.

**BRANDENBURG TELEPHONE COMPANY**  
**STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY**  
**FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>Common Stock</u>	<u>Retained Earnings</u>	<u>Other Comprehensive Income</u>	<u>Total</u>
Balance, December 31, 2009	\$ 5,000,000	\$ 34,251,452	\$ (2,732,232)	\$ 36,519,220
Comprehensive Income				
Net income for the year ended December 31, 2010	-0-	3,591,872	-0-	3,591,872
Change in Unrealized gains on marketable securities net of tax expense of \$7,163	-0-	-0-	10,307	10,307
Change in Pension Accrual net of tax expense of \$614,039	-0-	-0-	883,617	883,617
	<hr/>	<hr/>	<hr/>	<hr/>
Comprehensive Income	-0-	3,591,872	893,924	4,485,796
Cash Dividends:				
Common stock, \$25.00 per share to Holding Company	-0-	(5,000,000)	-0-	(5,000,000)
	<hr/>	<hr/>	<hr/>	<hr/>
Balance, December 31, 2010	5,000,000	32,843,324	(1,838,308)	36,005,016
Comprehensive Income				
Net income for the year ended December 31, 2011	-0-	4,767,113	-0-	4,767,113
Change in Unrealized gains on marketable securities net of tax expense of \$9,753	-0-	-0-	14,035	14,035
Change in Pension Accrual net of tax expense of \$2,131,063	-0-	-0-	(3,066,652)	(3,066,652)
	<hr/>	<hr/>	<hr/>	<hr/>
Comprehensive Income	-0-	4,767,113	(3,052,617)	1,714,496
Cash Dividends:				
Common stock, \$25.00 per share to Holding Company	-0-	(5,000,000)	-0-	(5,000,000)
	<hr/>	<hr/>	<hr/>	<hr/>
Balance, December 31, 2011	<u>\$ 5,000,000</u>	<u>\$ 32,610,437</u>	<u>\$ (4,890,925)</u>	<u>\$ 32,719,512</u>

See independent auditors' report.  
See notes to financial statements.

**BRANDENBURG TELEPHONE COMPANY**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
Cash Flows from Operating Activities:		
Cash received from regulated services	\$ 17,274,860	\$ 16,331,139
Other receipts	302,049	224,744
Cash paid to suppliers, employees, and affiliates	(8,552,932)	(10,291,226)
Interest received	36,899	10,677
Interest paid	(1,265)	(1,583)
Taxes paid	<u>(3,438,709)</u>	<u>(2,505,288)</u>
Net Cash Provided By Operating Activities	<u>5,620,902</u>	<u>3,768,463</u>
Cash Provided (Used) In Investing Activities:		
Construction and acquisition of telecommunications plant	(1,306,294)	(1,874,409)
Nonregulated activities	<u>1,833,778</u>	<u>2,112,717</u>
Net Cash Provided By Investing Activities	<u>527,484</u>	<u>238,308</u>
Cash Provided (Used) in Financing Activities:		
Dividends paid	(5,000,000)	(5,000,000)
(Decrease) in customer deposits	<u>(4,590)</u>	<u>-0-</u>
Net Cash Used In Financing Activities	<u>(5,004,590)</u>	<u>(5,000,000)</u>
Increase (Decrease) in Cash	1,143,796	(993,229)
Cash and Cash Equivalents Beginning of Year	<u>14,045,227</u>	<u>15,038,456</u>
<b>Cash and Cash Equivalents End of Year</b>	<b><u><u>\$ 15,189,023</u></u></b>	<b><u><u>\$ 14,045,227</u></u></b>

See independent auditors' report.

See notes to financial statements.

**BRANDENBURG TELEPHONE COMPANY**  
**STATEMENTS OF CASH FLOWS (CONTINUED)**  
**FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**

	<u>2011</u>	<u>2010</u>
Operating Activities:		
Net income	\$ 4,767,113	\$ 3,591,872
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,194,189	4,131,006
Deferred tax provisions	215,361	(410,785)
Decrease (Increase) in accounts receivable	(65,411)	(539,248)
Decrease (Increase) in income tax receivable	388,562	308,270
Decrease (Increase) in due from affiliate	(1,324,758)	11,407
Decrease (Increase) in materials inventory	163,895	337,734
Decrease (Increase) in prepaid insurance	53,310	5,157
Increase (Decrease) in accounts payable	252,726	73,944
Increase (Decrease) in customer deposits	(4,690)	(13,962)
Increase (Decrease) in accrued liabilities	(19,395)	(3,726,932)
	<u>5,620,902</u>	<u>3,768,463</u>
Net Cash Provided By Operating Activities	<u>\$ 5,620,902</u>	<u>\$ 3,768,463</u>

See independent auditors' report.

See notes to financial statements.

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2011 AND 2010**

**Note A - Summary of Significant Accounting Policies**

The Company maintains its records in accordance with practices prescribed or permitted by the Kentucky Public Service Commission and the Rural Utilities Service (RUS) which conforms to accounting principles generally accepted in the United States in all material respects. Accordingly, the Company follows these practices:

Nature of Operations:

The Brandenburg Telephone Company is a telephone company that offers business and residential telephone service to customers located in Meade, Hardin and Breckinridge counties in Kentucky.

Telephone Plant:

Telephone plant in service is stated at original cost, which is the cost when first dedicated to public service. Such cost includes applicable supervisory and overhead cost.

The cost of maintenance and repairs, including renewals of minor items of property, is charged to operating expense. The cost of depreciable property units, as distinguished from minor items, is charged to utility plant. The cost of removal, net of any salvage value, is charged to accumulated depreciation. Gain or loss on the sale of assets is recognized as income in the year in which the assets are sold.

Depreciation:

Provision has been made for depreciation for financial statement purposes on the basis of estimated useful lives of assets (as prescribed by the Public Service Commission of Kentucky) using the straight-line method.

Estimates:

Management uses estimates and assumptions in preparing these financial statements in accordance with U.S. generally accepted accounting principles. 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. Actual results could vary from the estimates that were used.

Accounts Receivable:

The Company considers its accounts receivable at cost less an allowance for doubtful accounts. On a periodic basis, the Company evaluates its accounts receivable and establishes an allowance for doubtful accounts, based on a history of past write-offs and collections and current credit conditions. The Company's policy is not to accrue interest on accounts receivable. Accounts are written off as uncollectible at the time management determines the collection is unlikely.

**Note B - Parent Subsidiary**

As of December 31, 2011, the Brandenburg Telephone Company is a wholly owned subsidiary of Brandenburg Communications Corporation.

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note C – Pension Plan**

The Company sponsors a defined benefit pension plan that covers substantially all employees. The plan calls for benefits to be paid to eligible employees at retirement based primarily upon years of service with the Company and compensation rates near retirement.

The following illustrates the pension plan for the year ended December 31, 2011 and 2010:

<b>Change in benefit obligation</b>	<u>2011</u>	<u>2010</u>
Benefit obligation at beginning of year	\$ 23,354,885	\$ 22,730,435
Service cost	717,637	645,367
Interest cost	1,139,561	1,083,328
Benefits paid	(732,559)	(592,767)
Actuarial (gain) or loss	<u>4,872,964</u>	<u>(511,478)</u>
Benefit obligation at end of year	<u>\$ 29,352,488</u>	<u>\$ 23,354,885</u>
 <b>Change in plan assets</b>		
Fair value of plan assets beginning of year	\$ 18,830,085	\$ 17,311,855
Actual return on plan assets	947,565	2,110,997
Employer contributions	-0-	-0-
Benefits paid	<u>(732,559)</u>	<u>(592,767)</u>
Fair value of plan assets at end of year	<u>\$ 19,045,091</u>	<u>\$ 18,830,085</u>
 <b>Reconciliation of funded status</b>		
Funded status	\$(10,307,397)	\$ (4,524,800)
Unrecognized actuarial (gain) or loss	-0-	-0-
Unrecognized transition (asset) or obligation	-0-	-0-
Unrecognized prior service cost	<u>-0-</u>	<u>-0-</u>
Net amount recognized at year-end	<u>\$(10,307,397)</u>	<u>\$ (4,524,800)</u>
 <b>Amounts recognized in the statement of financial position consist of:</b>		
Noncurrent liabilities	<u>\$(10,307,397)</u>	<u>\$ (4,524,800)</u>
Net amount recognized at year-end	<u>\$(10,307,397)</u>	<u>\$ (4,524,800)</u>
 <b>Amounts not yet reflected in net periodic benefit cost and included in accumulated other comprehensive income</b>		
Transition obligation asset (obligation)	\$ -0-	\$ -0-
Prior service credit (cost)	(51,844)	(58,178)
Accumulated gain (loss)	<u>(7,471,787)</u>	<u>(2,267,738)</u>
<b>Accumulated other comprehensive income (AOCI)</b>	<b>(7,523,631)</b>	<b>(2,325,916)</b>
Cumulative employer contributions in excess of net periodic benefit cost	<u>(2,783,766)</u>	<u>(2,198,884)</u>
Net amount recognized in statement of financial position	<u>\$(10,307,397)</u>	<u>\$ (4,524,800)</u>

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note C – Pension Plan (Continued)**

**Additional year-end information for plans  
with benefit obligations in excess of plan  
assets:**

	<u>2011</u>	<u>2010</u>
Benefit obligation	\$ 29,352,488	\$ 23,354,885
Fair value of plan assets	19,045,091	18,830,085

**Components of net periodic benefit cost**

Service cost	\$ 717,637	\$ 645,367
Interest cost	1,139,561	1,083,328
Expected return on plan assets	(1,278,650)	(1,176,116)
Amortization of prior service cost	6,334	6,334
Amortization of transitional obligation	-0-	(38,026)
Recognized actuarial (gain) loss	<u>-0-</u>	<u>82,989</u>
Net periodic benefit cost	<u>\$ 584,882</u>	<u>\$ 603,876</u>

**Weighted-average assumptions as of  
December 31**

	<u>2011</u>	<u>2010</u>
Discount rate	5.00%	5.00%
Expected return on plan assets	7.00%	7.00%
Rate of compensation increase	6.00%	6.00%

Following is an analysis of plan assets by category at measurement dates December 31:

	<u>2010</u>	<u>2009</u>
Cash	2%	2%
Debt Securities	28%	32%
Equity Securities	<u>70%</u>	<u>66%</u>
	<u>100%</u>	<u>100%</u>

Benefits expected to be paid in each of the next five years and in the aggregate for the five years thereafter are:

<u>Fiscal Year</u>	
2012	\$ 1,224,465
2013	1,251,519
2014	1,257,716
2015	1,291,500
2016	1,335,254
2017-2021	7,879,295

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note C – Pension Plan (Continued)**

To develop the expected long-term rate of return on assets assumption, the company considered the historical returns and the future expectations for returns for each asset class, as well as the target asset allocation of the pension portfolio. This resulted in the selection of the 7.00% long-term rate of return on assets assumption.

The Plan's investments are reported at fair value.

	<u>Fair Value</u>	<u>Fair Value Measurements Using:</u>	
		<u>Unadjusted Quoted Prices (Level 1)</u>	<u>Significant Other Observable Inputs (Level 2)</u>
<b>December 31, 2011</b>			
Common stocks	\$ 13,316,523	\$ 13,316,523	\$ -0-
Corporate bonds	3,289,764	-0-	3,289,764
U.S. government securities	2,086,401	-0-	2,086,401
Total	18,692,688	<u>\$ 13,316,523</u>	<u>\$ 5,376,165</u>
Cash accounts	352,403		
Total	<u>\$ 19,045,091</u>		

FASB ASC Topic 820, Fair Value Measurements and Disclosures, establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy consists of three broad levels: Level 1 inputs consist of unadjusted quoted prices in active markets for identical assets and have the highest priority, Level 2 inputs consists of observable inputs other than quoted market prices for identical assets, and Level 3 inputs have the lowest priority. The Plan uses appropriate valuation techniques based on the available inputs to measure the fair value of its investments. When available, the Plan measures fair value using Level 1 inputs because they generally provide the most reliable evidence of fair value.

*Level 1 Fair Value Measurements*

The fair values of common stock are based on quoted market prices.

*Level 2 Fair Value Measurements*

The fair value of corporate bonds and U.S. Government securities for which quoted market prices are not available are valued on yields currently available on comparable securities of issuers with similar credit ratings. Investments in certain restricted common stocks are valued at the quoted market price of the issuer's unrestricted common stock less an appropriate discount.

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note D - Cash Flow Information**

The Company considers all short-term investments with an original maturity of three months or less to be cash equivalents.

Cash paid for interest and income taxes for 2011 and 2010 was as follows:

	<u>2011</u>	<u>2010</u>
Interest paid	\$ <u>1,265</u>	\$ <u>1,583</u>
Income taxes	\$ <u>3,438,709</u>	\$ <u>2,505,288</u>

**Note E - Concentrations of Credit Risk**

The Company maintains cash and cash equivalents at several banks. The total cash balances at each bank are insured by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000. A summary of total insured and uninsured amounts held at these financial institutions at December 31, 2011 are as follows:

Total Cash and Cash Equivalents	\$ 15,165,235
Less: Balance Insured by FDIC	<u>1,000,000</u>
Uninsured and Uncollateralized	<u>\$ 14,165,235</u>

**Note F - Portfolio Investments**

In accordance with FASB ASC Topic 320, Investments – Debt and Equity Securities, the company has classified all the Other Investments as available-for-sale. Available-for-sale investments are stated at fair value with unrealized gains and losses included in stockholder's equities. The cost of investments sold is based on the specific identification method.

The cost and fair market values of marketable securities available for sale at December 31, 2011 and 2010 were:

	12/31/11	12/31/10
U.S. Government Securities:		
Amortized Cost	\$ 2,412,754	\$ 2,395,284
Gross Unrealized Gain	<u>23,788</u>	<u>17,470</u>
Fair Value	<u>\$ 2,436,542</u>	<u>\$ 2,412,754</u>

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note F – Portfolio Investments (Continued)**

At December 31, 2011, maturities of investments classified as available-for-sale were as follows:

	Amortized <u>Cost</u>	Fair <u>Value</u>
Less Than One Year	\$ 2,436,542	\$ 2,460,330
One Through Five Years	-0-	-0-
After Five Years	<u>-0-</u>	<u>-0-</u>
	<u>\$ 2,436,542</u>	<u>\$ 2,460,330</u>

The Plan's investments are reported at fair value in the accompanying statement of net assets available for benefit.

<u>December 31, 2011</u>	<u>Fair Value</u>	<u>Fair Value Measurements Using: Significant Other Observable Inputs (Level 2)</u>
Municipal bonds	\$ 2,215,995	\$ 2,215,995
Agency securities	<u>211,596</u>	<u>211,596</u>
Total	2,427,591	<u>\$ 2,427,591</u>
Cash accounts	<u>8,951</u>	
Total	<u>\$ 2,436,542</u>	

FASB ASC Topic 820, Fair Value Measurements and Disclosures, establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy consists of three broad levels: Level 1 inputs consist of unadjusted quoted prices in active markets for identical assets and have the highest priority, Level 2 inputs consists of observable inputs other than quoted market prices for identical assets, and Level 3 inputs have the lowest priority. The Plan uses appropriation valuation techniques based on the available inputs to measure the fair value of its investments. When available, the Plan measures fair value using Level 1 inputs because they generally provide the most reliable evidence of fair value.

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note F – Portfolio Investments (Continued)**

*Level 2 Fair Value Measurements*

The fair value of municipal bonds and agency securities for which quoted market prices are not available are valued on yields currently available on comparable securities of issuers with similar credit ratings. Investments in certain restricted common stocks are valued at the quoted market price of the issuer's unrestricted common stock less an appropriate discount.

**Note G – Comprehensive Income**

Comprehensive income is the total of (1) net income plus (2) all other changes in net assets arising from non-owner sources, which are referred to as other comprehensive income. The company has presented a statement of income that includes other comprehensive income. An analysis of changes in components of accumulated other comprehensive income is presented in the statement of changes in equity.

**Note H– Nonregulated Investments**

Investments in nonregulated activities consist of the following:

	<u>2011</u>	<u>2010</u>
Due from affiliate	\$ 410,066	\$ 415,633
Inventory	109,338	103,644
Land and land improvements	330,989	330,989
Other equipment	128,633	128,633
Fiber optic, mobile telephone and internet equipment	<u>2,392,315</u>	<u>4,023,508</u>
Total Nonregulated Investments	3,371,341	5,002,407
Less: Accumulated depreciation	2,252,248	4,012,706
Accounts payable	69,852	63,606
Accrued expenses	232,126	460,828
Other payable	<u>118,850</u>	<u>35,973</u>
	<u>\$ 698,265</u>	<u>\$ 429,294</u>

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note H– Nonregulated Investments (Continued)**

Following is a summary of net income from nonregulated investments for the year ending December 31, 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Income	\$ 3,916,359	\$ 4,387,366
Expenses	<u>1,813,609</u>	<u>2,288,798</u>
	<u>\$ 2,102,750</u>	<u>\$ 2,098,568</u>

Income tax expense related to these activities totaled \$882,396 in 2011 and \$1,142,554 in 2010.

**Note I – Telecommunications Plant:**

	<u>2011</u>	<u>2010</u>
Land	\$ 1,037,122	\$ 1,037,122
Buildings	9,126,013	9,110,284
Digital electronic equipment	24,210,674	24,098,921
Toll and subscriber carriers	2,917,825	2,885,854
Poles, cable and wire	28,927,332	28,026,252
Furniture and office equipment	3,812,917	3,711,020
Embedded accounts	300,712	300,712
Vehicles and other work equipment	<u>3,440,198</u>	<u>3,303,666</u>
Telephone plant in service	<u>\$ 73,772,793</u>	<u>\$ 72,473,831</u>

The Company provides depreciation on a straight-line basis at annual rates which will amortize the depreciable property over its estimated useful life. Such provision as a percentage of the average balance of the telephone plant in service was 6.9% in both 2011 and 2010. Individual plant depreciation rates are as follows:

	<u>Percent</u>
Buildings	2.7
Digital electronic equipment	7.5
Toll and subscriber equipment	11.9
Poles	5.6
Aerial cable – metallic	6.6
Aerial cable – fiber	5.1
Buried cable	5.5
Furniture	8.7
Computer equipment	15.8
Conduit Systems	2.2
Vehicles	12.1

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note J - Income Taxes and Deferred Income Taxes**

The Company and its parent file a consolidated federal income tax return. Income tax expense in the Company's income statement has been allocated an amount equal to the income tax that would have been applicable on a separate return basis.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amount of the Company's assets and liabilities for financial reporting basis and the amounts used for income tax purposes.

Deferred federal and state tax assets and liabilities in the accompanying balance sheet include the following:

	<u>2011</u>	<u>2010</u>
Deferred Tax Assets:		
Federal	\$ 7,214,947	\$ 7,239,733
State	<u>1,014,277</u>	<u>1,204,852</u>
Total Deferred Tax Assets	<u>8,229,224</u>	<u>8,444,585</u>
Net Deferred Benefit (Liability)	<u>\$ 8,229,224</u>	<u>\$ 8,444,585</u>
Current portion	\$ -0-	\$ -0-
Long-term portion	<u>8,229,224</u>	<u>8,444,585</u>
Net Deferred Tax Benefit (Liability)	<u>\$ 8,229,224</u>	<u>\$ 8,444,585</u>

Income taxes reflected in the Statement of Income include:

	<u>2011</u>	<u>2010</u>
Federal income taxes:		
Current tax expense	\$ 1,300,191	\$ 2,010,817
Deferred tax expense (benefit)	2,214,304	(1,015,651)
State income taxes:		
Current tax expense	262,730	429,167
Deferred tax expense (benefit)	<u>205,244</u>	<u>3,513</u>
Total income tax expense	<u>\$ 3,982,469</u>	<u>\$ 1,427,846</u>

The principal sources of temporary differences are different depreciation methods used for financial accounting and tax purposes, as well as pension expense.

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note K - Related Party Transactions:**

Brandenburg Telephone Company has certificates of deposit at Meade County Bank and West Point Bank, as follows:

<u>Bank</u>	<u>Date</u>	<u>Maturity Date</u>	<u>Certificate Number</u>	<u>Interest Rate</u>	<u>Amount</u>
Meade County	2/11/06	2/11/12	5547	0.750%	\$ 996,939
West Point	1/27/06	1/13/12	0058	1.002%	\$ 912,697

In addition, the Company has money market and operating accounts in the following banks:

<u>Bank</u>	<u>Amount</u>
<u>Operating Accounts:</u>	
Meade County	\$ 1,291,142
First State	3,338,043
West Point	<u>5,946,453</u>
Total Operating Accounts	<u>\$ 10,575,638</u>
<u>Money Market Accounts:</u>	
First State	\$ 986,977
River City	<u>1,689,183</u>
Total Money Market Accounts	<u>\$ 2,676,160</u>

Meade County Bank, West Point Bank, River City Bank, First State Bank and Brandenburg Telephone Company are related by common ownership.

During 2001, Brandenburg Telecom, LLC (the Corporation), a wholly-owned subsidiary of Brandenburg Communications Corporation was formed. The Corporation will provide telecommunication services in Elizabethtown, Kentucky and other areas outside the franchise territory of Brandenburg Telephone Company. Brandenburg Telephone Company provided the Corporation with funding to assist the Corporation's organizational expenditures. As of December 31, 2011, the amount due to Brandenburg Telephone Company was \$12,655,607.

**Note L - Subsequent Event Policy**

Brandenburg Telephone Company has evaluated subsequent events through March 20, 2012, the date which the financial statements were available to be issued.

**BRANDENBURG TELEPHONE COMPANY**  
**NOTES TO FINANCIAL STATEMENTS (CONTINUED)**  
**DECEMBER 31, 2011 AND 2010**

**Note M – Accounting for Uncertain Tax Positions**

The company adopted the accounting standard regarding “Accounting for Uncertain Tax Positions”. This standard provides detailed guidance for financial statement recognition, measurement, and disclosure of uncertain tax positions recognized in the enterprise’s financial statements. It requires an entity to recognize the financial statement benefit of a tax position when it is more likely than not that the position will be sustained upon examination. The adoption of this standard had no material effect on the Company’s financial position, results of operations, or cash flow. The tax years of 2008-2011 remain subject to examination by taxing authorities.

William A. Talley  
Jon D. Chesser  
Bob E. Wientjes

Kentucky Offices:  
Louisville  
Brandenburg  
Bardstown

**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***

The Board of Directors  
Brandenburg Telephone Company  
Brandenburg, KY 40108

We have audited the financial statements of the Brandenburg Telephone Company, as of and for the years ended December 31, 2011 and 2010, and have issued our report thereon dated March 20, 2012. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Brandenburg Telephone Company'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 and the Rural Telephone Bank and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Richardson, Pennington & Skinner, PSC

Louisville, Kentucky  
March 20, 2012