

**SOUTHERN TIER NETWORK, INC.**

**Financial Statements  
as of December 31, 2013 and 2012  
Together with  
Independent Auditor's Report**

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

## INDEPENDENT AUDITOR'S REPORT

March 12, 2014

To the Board of Directors of the  
Southern Tier Network, Inc.:

### **Report on the Financial Statements**

We have audited the accompanying financial statements of Southern Tier Network, Inc., which comprise the balance sheets as of December 31, 2013 and 2012, and the related statements of activities and change in net assets and cash flows for the years then ended, and the related notes to the financial statements.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Southern Tier Network, Inc. as of December 31, 2013 and 2012, and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States.

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## INDEPENDENT AUDITOR'S REPORT

(Continued)

### **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated March 12, 2014 on our consideration of Southern Tier Network, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Southern Tier Network, Inc.'s internal control over financial reporting and compliance.

Bonadio & Co., LLP

# SOUTHERN TIER NETWORK, INC.

## BALANCE SHEETS DECEMBER 31, 2013 AND 2012

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|                                   | <u>2013</u>          | <u>2012</u>          |
|-----------------------------------|----------------------|----------------------|
| <b>ASSETS</b>                     |                      |                      |
| OTHER ASSETS:                     |                      |                      |
| Cash                              | \$ 1,735,151         | \$ 1,939,132         |
| Contributions receivable          | 2,762,790            | 5,762,790            |
| Accounts receivable               | 182,405              | 117,125              |
| Prepaid expenses                  | <u>7,703</u>         | <u>7,982</u>         |
| Total other assets                | <u>4,688,049</u>     | <u>7,827,029</u>     |
| FIXED ASSETS:                     |                      |                      |
| Fiber optic cable plant           | 6,044,681            | 645,999              |
| Construction in progress          | 497,665              | 2,163,790            |
| Parts and supplies inventory      | <u>191,382</u>       | <u>515,863</u>       |
|                                   | 6,733,728            | 3,325,652            |
| Less: Accumulated depreciation    | <u>(157,062)</u>     | <u>(9,421)</u>       |
| Net fixed assets                  | <u>6,576,666</u>     | <u>3,316,231</u>     |
|                                   | <u>\$ 11,264,715</u> | <u>\$ 11,143,260</u> |
| <b>LIABILITIES AND NET ASSETS</b> |                      |                      |
| LIABILITIES:                      |                      |                      |
| Accounts payable                  | \$ 461,675           | \$ 631,034           |
| Deferred installation revenue     | <u>1,101,174</u>     | <u>101,400</u>       |
| Total liabilities                 | <u>1,562,849</u>     | <u>732,434</u>       |
| NET ASSETS:                       |                      |                      |
| Unrestricted                      | 7,001,866            | 4,710,826            |
| Temporarily restricted            | <u>2,700,000</u>     | <u>5,700,000</u>     |
| Total net assets                  | <u>9,701,866</u>     | <u>10,410,826</u>    |
| Total liabilities and net assets  | <u>\$ 11,264,715</u> | <u>\$ 11,143,260</u> |

The accompanying notes are an integral part of these statements.

**SOUTHERN TIER NETWORK, INC.**

**STATEMENTS OF ACTIVITIES AND CHANGE IN NET ASSETS  
FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012**

|                                       | 2013                |                        | 2012                |                     |                        |                      |
|---------------------------------------|---------------------|------------------------|---------------------|---------------------|------------------------|----------------------|
|                                       | Unrestricted        | Temporarily Restricted | Total               | Unrestricted        | Temporarily Restricted | Total                |
| <b>SUPPORT AND REVENUE:</b>           |                     |                        |                     |                     |                        |                      |
| Contributions                         | \$ 326,106          | -                      | \$ 326,106          | \$ 1,433,892        | -                      | \$ 1,433,892         |
| Service revenue                       | 184,756             | -                      | 184,756             | 13,125              | -                      | 13,125               |
| Installation revenue                  | 62,166              | -                      | 62,166              | 2,600               | -                      | 2,600                |
| Interest income                       | 2,878               | -                      | 2,878               | 86                  | -                      | 86                   |
| Release from restriction              | 3,000,000           | (3,000,000)            | -                   | 3,000,000           | (3,000,000)            | -                    |
| <b>Total support and revenue</b>      | <b>3,575,906</b>    | <b>(3,000,000)</b>     | <b>575,906</b>      | <b>4,449,703</b>    | <b>(3,000,000)</b>     | <b>1,449,703</b>     |
| <b>EXPENSES:</b>                      |                     |                        |                     |                     |                        |                      |
| Network operations                    | 664,375             | -                      | 664,375             | 261,312             | -                      | 261,312              |
| Support services                      | 235,116             | -                      | 235,116             | 107,468             | -                      | 107,468              |
| Depreciation                          | 147,641             | -                      | 147,641             | 9,421               | -                      | 9,421                |
| Administrative                        | 126,063             | -                      | 126,063             | 107,576             | -                      | 107,576              |
| Professional fees                     | 88,601              | -                      | 88,601              | 28,177              | -                      | 28,177               |
| Insurance                             | 21,835              | -                      | 21,835              | 35,573              | -                      | 35,573               |
| Office and supplies                   | 1,235               | -                      | 1,235               | 1,422               | -                      | 1,422                |
| <b>Total expenses</b>                 | <b>1,284,866</b>    | <b>-</b>               | <b>1,284,866</b>    | <b>550,949</b>      | <b>-</b>               | <b>550,949</b>       |
| <b>CHANGE IN NET ASSETS</b>           | <b>2,291,040</b>    | <b>(3,000,000)</b>     | <b>(708,960)</b>    | <b>3,898,754</b>    | <b>(3,000,000)</b>     | <b>898,754</b>       |
| <b>NET ASSETS - beginning of year</b> | <b>4,710,826</b>    | <b>5,700,000</b>       | <b>10,410,826</b>   | <b>812,072</b>      | <b>8,700,000</b>       | <b>9,512,072</b>     |
| <b>NET ASSETS - end of year</b>       | <b>\$ 7,001,866</b> | <b>\$ 2,700,000</b>    | <b>\$ 9,701,866</b> | <b>\$ 4,710,826</b> | <b>\$ 5,700,000</b>    | <b>\$ 10,410,826</b> |

The accompanying notes are an integral part of these statements.

## SOUTHERN TIER NETWORK, INC.

### STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2013 AND 2012

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|   | <u>2013</u>         | <u>2012</u>         |
|---|---------------------|---------------------|
| CASH FLOW FROM OPERATING ACTIVITIES:  |                     |                     |
| Change in net assets  | \$ (708,960)        | \$ 898,754          |
| Adjustments to reconcile change in net assets to net cash flow from operating activities: |                     |                     |
| Contributions - cash received   | (3,326,106)         | (4,371,102)         |
| Depreciation  | 147,641             | 9,421               |
| Changes in:   |                     |                     |
| Contribution receivable   | 3,000,000           | 2,937,210           |
| Accounts receivable   | (65,280)            | (117,125)           |
| Prepaid expense   | 279                 | (694)               |
| Accounts payable  | (578,867)           | 5,652               |
| Deferred installation revenue   | <u>999,774</u>      | <u>101,400</u>      |
| Net cash flow from operating activities   | <u>(531,519)</u>    | <u>(536,484)</u>    |
| CASH FLOW FROM INVESTING ACTIVITIES:  |                     |                     |
| Purchases of property and equipment   | <u>(2,998,568)</u>  | <u>(2,621,129)</u>  |
| Net cash flow from investing activities   | <u>(2,998,568)</u>  | <u>(2,621,129)</u>  |
| CASH FLOW FROM FINANCING ACTIVITIES:  |                     |                     |
| Contributions - cash received   | <u>3,326,106</u>    | <u>4,371,102</u>    |
| Net cash flow from financing activities   | <u>3,326,106</u>    | <u>4,371,102</u>    |
| CHANGE IN CASH  | (203,981)           | 1,213,489           |
| CASH - beginning of year  | <u>1,939,132</u>    | <u>725,643</u>      |
| CASH - end of year  | <u>\$ 1,735,151</u> | <u>\$ 1,939,132</u> |

#### NON CASH OPERATING AND INVESTING ACTIVITIES:

Non cash operating and investing activities related to property and equipment purchases included in accounts payable at December 31, 2013 and 2012 were \$409,508 and \$590,031, respectively.

The accompanying notes are an integral part of these statements.

# SOUTHERN TIER NETWORK, INC.

## NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2013 AND 2012

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### 1. THE ORGANIZATION

Southern Tier Network, Inc. (STN) is a not-for profit, local development corporation (LDC) based in Corning, New York and formed to provide stewardship for the construction and management of a whole-sale, Municipal Based Open Access optical fiber telecommunications system and promote economic development within Steuben, Schuyler, and Chemung counties. The network will connect the three counties and create an environment for improved telecommunications competition, reliability and diversity. STN will do so by leasing high speed fiber optic capacity to enterprise, carrier, and other entities that desire to manage and control their own telecommunications services. This network will aid economic development by attracting new business, improving communications among health care providers and educational institutions, supporting individual county emergency services E-911 communications systems, and partnering with private enterprises.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### **Basis of Accounting**

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

#### **Financial Reporting**

STN reports its activities and related net assets using the following net asset classifications:

- Unrestricted net assets include resources that are available for the support of STN's operating activities and net investment in property and equipment.
- Temporarily restricted net assets include resources that have been contributed to STN subject to certain time restrictions, as defined by the donor.

#### **Cash**

Cash consists of three bank accounts which, at times, may exceed federally insured limits. STN has not experienced any losses in these accounts and believes it is not exposed to any significant credit risk with respect to cash.

#### **Contribution Receivable**

STN records contribution receivable and contribution revenue when an unconditional promise to give is received. STN records an allowance for doubtful accounts in anticipation of future write-offs to the extent deemed necessary based on past experience. At December 31, 2013 and 2012, no allowance was considered necessary.

#### **Accounts Receivable**

STN extends credit to its customers. Accounts receivable are stated at the amount billed. At December 31, 2013 and 2012, no allowance was considered necessary. Receivables are considered impaired if full principal payments are not received in accordance with the contractual terms. It is STN's policy to charge off uncollectible contracts receivable when management determines the receivable will not be collected.

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

### **Fixed Assets**

Fixed assets are stated at cost or, if donated, at fair value at the date of donation. STN capitalizes fixed asset purchases greater than \$5,000 that have useful lives greater than one year. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Construction-in-progress is recognized as the accumulation of costs related to fixed assets through the date that the fixed assets are placed in service. Depreciation and amortization are provided on the straight-line basis over the estimated useful lives, which range from three to twenty-five years.

### **Deferred Installation Revenue**

Deferred installation revenue represents amounts received from customers related to each customer's initial connection to STN's fiber optic network. These amounts are deferred and recognized as revenue on a straight-line basis over the terms of each customer's lease for access to the network, all of which are currently ten years.

### **Income Taxes**

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

For tax-exempt entities, their tax-exempt status itself is deemed to be an uncertainty, since events could potentially occur to jeopardize their tax-exempt status. As of December 31, 2013 and 2012, STN does not have a liability for unrecognized tax benefits, nor does it file federal or New York State income tax returns.

### **Reclassifications**

Certain amounts have been reclassified in the prior year financial statements to conform to the current year presentation.

### **Estimates**

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

## **3. ADMINISTRATIVE SERVICES**

STN has contracted with Southern Tier Central Regional Planning and Development Board (STC) to provide management, accounting and specialist services. STC's Executive Director is the Chair of the Board of STN. Approximately \$126,000 and \$108,000 was recognized as expense under the terms of the agreement during 2013 and 2012, respectively.

## **4. TEMPORARILY RESTRICTED NET ASSETS**

STN's temporarily restricted net assets are restricted for STN's initial capital costs for the construction of the fiber optic ring, as well as operating cash flow needs during the construction period.



## 5. CONTRIBUTION AND CONTRIBUTION RECEIVABLE

STN's contribution income was 100% and 99% from Steuben, Schuyler, and Chemung Counties, respectively, for the years ended December 31, 2013 and 2012.

STN's contribution receivable was 92% and 99%, respectively, due from Corning, Inc. at December 31, 2013 and 2012. There is no set schedule for when payments related to this contribution receivable will be received. The arrangement allows for STN to request and receive cash payments on the contribution receivable as STN's cash flow needs dictate.

## 6. CUSTOMER ARRANGEMENTS

### Deferred Installation Revenue

STN enters into agreements with customers to provide access to STN's fiber optic network. Certain agreements require customers to make up-front payments related to establishing their connection to the fiber optic network. These up-front payments have been recorded as deferred revenue and are being recognized as income using the straight-line method over the terms of the agreements. Agreements in place through December 31, 2013 have terms ranging from five to ten years, with the latest expiring in October 2023.

As of December 31, 2013, deferred revenue is to be recognized as income in the following years:

|            |    |                  |
|------------|----|------------------|
| 2014       | \$ | 127,798          |
| 2015       |    | 127,798          |
| 2016       |    | 127,798          |
| 2017       |    | 127,798          |
| 2018       |    | 126,864          |
| Thereafter |    | <u>463,118</u>   |
|            | \$ | <u>1,101,174</u> |

### Future Lease Payments to be Received

STN leases continuing use of its fiber optic network under the terms of non-cancellable customer agreements requiring monthly payments for terms of up to ten years. Payments to be received under the terms of these agreements are as follows for the years ending December 31:

|            |    |                  |
|------------|----|------------------|
| 2014       | \$ | 127,188          |
| 2015       |    | 127,188          |
| 2016       |    | 127,188          |
| 2017       |    | 127,188          |
| 2018       |    | 127,188          |
| Thereafter |    | <u>635,940</u>   |
|            | \$ | <u>1,271,880</u> |

## 7. FUNCTIONAL EXPENSES

STN's expenses on a functional basis are as follows for the years ended December 31, 2013 and 2012.

|                            | <u>2013</u>         | <u>2012</u>       |
|----------------------------|---------------------|-------------------|
| Program operations         | \$ 1,045,422        | \$ 373,171        |
| General and administrative | <u>239,444</u>      | <u>177,778</u>    |
|                            | <u>\$ 1,284,866</u> | <u>\$ 550,949</u> |

## 8. CONTINGENCY

On February 8, 2012, STN entered into an irrevocable standby letter of credit with a financial institution for \$75,000 at 1.25% interest, with an unrelated beneficiary. This letter of credit was required as an element of on-going construction activities. This letter of credit has been renewed through February 8, 2015

## 9. SUBSEQUENT EVENTS

Subsequent events have been evaluated through March 12, 2014, which is the date the financial statements were available to be issued.

On January 10, 2014, STN received a payment of \$2,000,000 on the contribution receivable in the normal course of the contributor's provision of cash for operating expenses and capital expenditures.

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

March 12, 2014

To the Board of Directors of  
Southern Tier Network, Inc.:

We have audited, in accordance with the auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Southern Tier Network, Inc., which comprise the balance sheet as of December 31, 2013, and the related statements of activities and change in net assets, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 12, 2014.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered Southern Tier Network, Inc.'s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Southern Tier Network, Inc.'s internal control. Accordingly, we do not express an opinion on the effectiveness of Southern Tier Network, Inc.'s internal control.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. *A material weakness* is a deficiency, or a 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. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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

(Continued)

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether Southern Tier Network, Inc.'s financial statements are free from 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*.

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Bonadio & Co., LLP