

Consolidated Communications Holdings, Inc.

Form 10-K

March 08, 2010

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549  
FORM 10-K**

[Mark One]

**Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended December 31, 2009**

**OR**

**Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from \_\_\_\_\_ to \_\_\_\_\_.**

**Commission file number 000-51446**

**CONSOLIDATED COMMUNICATIONS HOLDINGS, INC.**

(Exact name of registrant as specified in its charter)

Delaware

02-0636095

(State or other jurisdiction of  
incorporation or organization)

(IRS Employer Identification No.)

121 South 17<sup>th</sup> Street  
Mattoon, Illinois

61938

(Address of principal executive offices)

(Zip Code)

(217) 235-3311

(Registrant's Telephone Number, including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class:

Name of exchange on which registered:

Common Stock, \$0.01 par value

NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES  NO

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. YES  NO

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES  NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES  NO

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form

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10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting  
company

(Do not check if a smaller  
reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  
YES  NO

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant as of June 30, 2009 was approximately \$271,905,064 based upon the closing price of the Common Stock reported for such date on the NASDAQ Global Select Market.

Indicate the number of shares outstanding of each class of Common Stock, as of the latest practicable date:

Class	Outstanding as of March 3, 2010
Common Stock, \$0.01 par value	29,608,653 Shares

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the definitive proxy statement for the annual meeting of stockholders to be held on May 4, 2010 are incorporated by reference into Part III.

**FORM 10-K**  
**YEAR ENDED DECEMBER 31, 2009**  
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**Acronyms Used in this Annual Report on Form 10-K**

ARPU	Average revenue per user
CLEC	Competitive local exchange carrier
CSA	Carrier serving area
DSL	Digital subscriber line
DVR	Digital video recorder
EBITDA	Earnings before interest, taxes, depreciation and amortization
ETFL	East Texas Fiber Line, Inc.
FASB	Financial Accounting Standards Board
FCC	Federal Communications Commission
GAAP	Generally accepted accounting principles
HD	High definition
ICC	Illinois Commerce Commission
ICTC	Illinois Consolidated Telephone Company
ILEC	Incumbent local exchange carrier
IP	Internet protocol
IPO	Initial public offering
IPTV	Internet protocol digital television
ISP	Internet service provider
LIBOR	London interbank offer rate
mbps	megabit per second
MPLS	Multi-protocol label switching
NECA	National Exchange Carrier Association
NOC	Network operations center
NOL	Net operating loss
PAPUC	Pennsylvania Public Utility Commission
PAUSF	Pennsylvania Universal Service Fund
PUCT	Public Utility Commission of Texas
PURA	Texas Public Utilities Regulatory Act
RBOC	Regional Bell Operating Company
RLEC	Rural local exchange carrier
SONET	Synchronous Optical Network
SPCOA	Service Provider Certificate of Operating Authority
TXUCV	TXU Communications Ventures Company
UNE	Unbundled network element
UNE-P	Unbundled network element platform
VOIP	Voice over Internet Protocol
WACC	Weighted-average cost of capital

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**Terminology Used in this Annual Report on Form 10-K**

***Access line equivalents*** represent a combination of voice services and data circuits. The calculations represent a conversion of data circuits to an access line basis. Equivalents are calculated by converting data circuits (basic rate interface (BRI), primary rate interface (PRI), DSL, DS-1, DS-3, and Ethernet) and SONET-based (optical) services (OC-3 and OC-48) to the equivalent of an access line.

***Competitive local exchange carriers*** (CLECs) are telecommunications providers formed after enactment of the Telecommunications Act of 1996 to provide local exchange service that competes with ILECs and other established carriers.

***Digital telephone or VOIP service*** involves the routing of voice calls, at least in part, over the Internet through packets of data instead of transmitting the calls over the telephone system.

An ***exchange*** is a geographic area established for administration and pricing of telecommunications services.

***Hosted VOIP*** is our broadband phone product that utilizes our soft switch to provide an Internet Protocol based voice service to business and residential customers. The product provides the flexibility of utilizing new telephone technology and features provided by our hosted soft switch but does not require an investment in a new telephone system to use the advanced features.

***Incumbent local exchange telephone companies*** (ILECs) are the local telephone companies that provided local telephone exchange service on the effective date of the Telecommunications Act of 1996, or their predecessors. This designation is important because ILECs have statutory obligations that other telephone companies do not have. For example, ILECs are required to give other carriers access to certain equipment (known as unbundled network elements) or to house equipment for other carriers (known as collocation), on reasonable and nondiscriminatory terms. For more information, see Part I Item 1 Business Regulatory Environment.

***Metro Ethernet*** is the use of carrier Ethernet technology in metropolitan area networks. Metro Ethernet services are provided over a standard, widely used Ethernet interface and can connect business local area networks to wide area networks or to the Internet. Metro Ethernet offers cost-effectiveness, reliability, scalability and bandwidth management superior to most proprietary networks.

***MPLS or Multiprotocol Label Switching*** refers to a highly scalable data-carrying mechanism in which data packets are assigned labels. Packet-forwarding decisions are made solely on the contents of this label, without the need to examine the packet itself. This allows for end-to-end circuits across any type of transport medium, using any protocol.

***Rural telephone companies*** provide communications services to geographic areas that are not heavily populated. This designation is important because rural telephone companies are eligible to receive government subsidies to compensate for the disproportionate cost of providing service in low density areas. In addition, ILECs that are statutory rural telephone companies, as defined in the Telecommunications Act of 1996, are exempt from some obligations to provide access to competitors.

***Unified messaging*** is the integration of multiple messaging technologies into a single system. With this application, voice mail, fax, cellular and other messages are sent to the email inbox. From the email system, the messages can be heard, read or forwarded to others.

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**FORWARD-LOOKING STATEMENTS**

Any statements contained in this report that are not statements of historical fact, including statements about our beliefs and expectations, are forward-looking statements. We use words like anticipate, believe, expect, intend, estimate, target, project, should, may, and will to identify forward-looking statements throughout this report. Forward-looking statements reflect, among other things, our current expectations, plans, strategies, and anticipated financial results. There are a number of risks, uncertainties, and conditions that may cause our actual results to differ materially from those expressed or implied by these forward-looking statements. Many of these circumstances are beyond our ability to control or predict. Moreover, forward-looking statements necessarily involve assumptions on our part.

All forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the cautionary statements that appear throughout this report. Furthermore, forward-looking statements speak only as of the date they are made. Except as required under the federal securities laws or the rules and regulations of the Securities and Exchange Commission, we are not under any obligation to update any forward-looking information whether as a result of new information, future events, or otherwise. You should not place undue reliance on forward-looking statements.

Please see Part I Item 1A Risk Factors of this report, as well as the other documents that we file with the SEC from time to time, for important factors that could cause our actual results to differ from current expectations and from the forward-looking statements discussed in this report.

**MARKET AND INDUSTRY DATA**

Market and industry data and other information used throughout this report are based on independent industry publications, government publications, publicly available information, reports by market research firms, or other published independent sources. Although we believe these sources are reliable, we have not verified the information. Some data is also based on estimates that members of management derive from their industry knowledge and review of internal surveys.

We cannot know, or reasonably determine, our market share in each of our markets or for our services because there is significant overlap in the telecommunications industry; it is difficult to isolate information regarding individual services. For example, wireless providers both compete with and complement our local telephone services.



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**PART I**

**Item 1. Business**

**General**

Consolidated Communications Holdings, Inc. and its subsidiaries, ( Consolidated , the Company , we , our or ) operates its businesses under the name Consolidated Communications. We are an established rural local exchange carrier ( RLEC ) providing communications services to residential and business customers in Illinois, Texas and Pennsylvania. With 247,235 local access lines, an estimated 72,681 Competitive Local Exchange Carrier ( CLEC ) access line equivalents, 100,122 digital subscriber lines ( DSL ) and 23,127 Internet Protocol digital television ( IPTV ) subscribers at December 31, 2009, we believe that we are one of the largest pure play RLECs in the United States. The Company offers a wide range of telecommunications services, including local and long-distance service, digital telephone service ( VOIP ), custom calling features, private line services, dial-up and high-speed broadband Internet access, IPTV, carrier access services, network capacity services over our regional fiber optic network, directory publishing and CLEC calling services. We also operate a number of non-core complementary businesses, including providing telephone services to county jails and state prisons and equipment sales. See Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Subsequent Events .

Founded in 1894 as the Mattoon Telephone Company by the great-grandfather of our current Chairman, Richard A. Lumpkin, we began as one of the nation's first independent telephone companies. After several acquisitions, the Mattoon Telephone Company was incorporated as the Illinois Consolidated Telephone Company ( ICTC ) on April 10, 1924. In 1997, McLeodUSA acquired ICTC and all related businesses from the Lumpkin family. In 2002, Mr. Lumpkin and two private equity firms, Spectrum Equity and Providence Equity, repurchased ICTC and several related businesses.

On April 14, 2004, we acquired TXU Communications Ventures Company ( TXUCV ) from TXU Corporation. TXUCV owned rural telephone operations in Lufkin, Conroe, and Katy, Texas, which had been operating in those markets for over 90 years. This acquisition approximately tripled the size of the Company.

On July 27, 2005, we completed an initial public offering of our common stock. At the same time, Spectrum Equity sold its entire investment and Providence Equity sold 50% of its investment. In July 2006, we repurchased the remaining shares owned by Providence Equity.

On December 31, 2007, we acquired all of the capital stock of North Pittsburgh Systems, Inc. ( North Pittsburgh ). Through its subsidiaries, North Pittsburgh provides advanced communication services to residential and business customers in several counties in western Pennsylvania and operates a CLEC in the Pittsburgh metropolitan area. The results of operations for North Pittsburgh are included in the Company's Telephone Operations segment beginning January 1, 2008 and thereafter.

We are a Delaware corporation organized in 2002, and are the successor to businesses engaged in providing telecommunications services since 1894.

**Table of Contents****Available Information**

Our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports are available on our website, at no charge, at [www.consolidated.com](http://www.consolidated.com), as soon as reasonably practicable after electronic filing or furnishing such information to the U.S. Securities and Exchange Commission ( SEC ). Also available on our website, or in print upon written request at no charge, are our corporate governance guidelines, the charters of our audit, compensation and corporate governance committees, and a copy of our code of business conduct and ethics that applies to our directors, officers and employees, including our chief executive officer, principal financial officer, principal accounting officer, controller or other persons performing similar functions. Information on our website should not be considered to be part of this annual report on Form 10-K.

**Business Overview**

We derive our revenue principally from the sale of telecommunication services, including local and long-distance telephone (both traditional telephone service and VOIP), high-speed broadband Internet, and standard and high-definition IPTV services to residential and business customers in Illinois, Texas and Pennsylvania. We also derive revenues from a number of complementary non-core businesses, including telephone services to county jails and state prisons; equipment sales; and prior to 2010, telemarketing and order fulfillment and operator services. We operate in two reportable segments: Telephone Operations and Other Operations. Our Telephone Operations segment generates the substantial majority of our revenue and operating income and substantially all of our cash flow from operations.

*Sources of Revenue*

The following chart summarizes our sources of revenue for the last three years:

<i>(in millions, except for percentages)</i>	2009		2008		2007	
	\$	% of Revenues	\$	% of Revenues	\$	% of Revenues
Telephone operations:						
Local calling services	<b>97.2</b>	<b>23.9</b>	104.6	25.0	82.8	25.2
Network access services	<b>86.3</b>	<b>21.3</b>	95.3	22.8	70.9	21.5
Subsidies	<b>56.0</b>	<b>13.8</b>	55.2	13.2	46.0	14.0
Long-distance services	<b>20.4</b>	<b>5.0</b>	24.1	5.7	14.2	4.3
Data and Internet services	<b>68.1</b>	<b>16.8</b>	62.7	15.0	38.0	11.5
Other services	<b>36.6</b>	<b>9.0</b>	37.1	8.9	36.3	11.0
Total telephone operations	<b>364.6</b>	<b>89.8</b>	379.0	90.6	288.2	87.5
Other operations	<b>41.6</b>	<b>10.2</b>	39.4	9.4	41.0	12.5
Total operating revenue	<b>406.2</b>	<b>100.0</b>	418.4	100.0	329.2	100.0

**Table of Contents***Telephone Operations*

Our Telephone Operations segment consists of local calling services, network access services, subsidies, long-distance services, data and Internet services (including DSL, IPTV and VOIP), and other services. Our Telephone Operations segment had the following service lines as of December 31:

	2009	December 31, 2008	2007
Residential access lines in service	146,766	162,067	183,070
Business access lines in service	100,469	102,256	103,116
Total local access lines in service	247,235	264,323	286,186
VOIP telephone subscribers	8,665	6,510	2,494
IPTV subscribers	23,127	16,666	12,241
ILEC DSL subscribers	100,122	91,817	81,337
Total broadband connections	131,914	114,993	96,072
CLEC access line equivalents <sup>(1)</sup>	72,681	74,687	70,063
Total connections	451,830	454,003	452,321
Long-distance lines <sup>(2)</sup>	165,714	165,953	166,599
Dial-up subscribers	2,371	3,957	5,578

(1) CLEC access line equivalents represent a combination of voice services and data circuits. The calculations represent a conversion of data circuits to an access line basis. Equivalents are calculated by converting data circuits (basic rate interface, primary rate interface, DSL, DS-1, DS-3 and Ethernet) and SONET-based

(optical) services  
(OC-3 and  
OC-48) to the  
equivalent of an  
access line.

- (2) Reflects the  
inclusion of  
long-distance  
service provided  
as part of our  
VOIP offering  
while excluding  
CLEC  
long-distance  
subscribers.

Our Telephone Operations segment generated approximately \$115.8 million and \$91.9 million of cash flows from operating activities for the years ended December 31, 2009 and 2008, respectively. As of December 31, 2009, our Telephone Operations had total assets of approximately \$1.2 billion.

Local calling services

These services include dial tone and other basic services. We generally charge residential and business customers a fixed monthly rate for access to the network and for originating and receiving telephone calls within their local calling area.

Custom calling features include caller name and number identification, call forwarding, and call waiting. Value-added services include teleconferencing and voice mail. We usually charge a flat monthly fee for custom calling features and value-added services. Otherwise, we bundle the selected services with local calling services at a discounted rate.

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We offer private lines that provide direct connections between two or more local locations primarily to business customers at flat monthly rates. In our Pennsylvania and Texas markets, we offer small- and medium-sized businesses a hosted VOIP package, which utilizes our current switch and allows the customer the flexibility of utilizing new telephone technology and features without investing in a new telephone system to get the features. The package bundles local service, calling features, IP business telephones, and unified messaging, which integrates multiple messaging technologies into a single system, such as allowing the customer to receive and listen to voice messages through email. We also offer a similar product to our residential customers in Texas, Pennsylvania and Illinois.

**Network access services**

A significant portion of our revenue comes from network access charges paid by long-distance and other carriers for originating or terminating calls within our service areas. These services allow customers to make or receive calls in our service area. Our long-distance customers typically pay a monthly fee for this service. In addition, other carriers pay network access charges for originating or terminating calls within our service areas. These charges, which are regulated, also apply to private lines that connect a customer in one of our service areas to a location outside of our service areas. Network access charges include subscriber line charges (a fee for being connected to the telephone network), local number portability fees (whereby consumers can keep their telephone number when changing carriers), and universal services surcharges, as well as the costs of originating and terminating calls from or to our local exchanges. The amount of network access charge revenues we receive is based on rates set or approved by federal and state regulatory commissions that are subject to change at any time.

We record the details of long-distance and switched access calls through our carrier access billing system and bill the applicable carriers on a monthly basis. The network access charge rates for intrastate long-distance calls and private lines within Illinois, Texas, and Pennsylvania are regulated and approved by the Illinois Commerce Commission ( ICC ), the Public Utility Commission of Texas ( PUCT ), and the Pennsylvania Public Utility Commission ( PAPUC ) respectively. The access charge rates for interstate long-distance calls and private lines are regulated and approved by the Federal Communications Commission ( FCC ). See Regulatory Environment Federal Regulation and Regulatory Environment Access Charges.

**Subsidies**

Subsidies consist of federal and state subsidies designed to promote widely available, quality telephone service at affordable prices in rural areas. Subsidies come from pools to which we and other telecommunications providers, including local, long-distance, and wireless carriers, contribute on a monthly basis. Subsidies are allocated and distributed to rural carriers monthly based upon their respective costs for providing local service. Like access charges, subsidies are regulated by federal and state regulatory commissions. In Illinois, we receive federal but not state subsidies. In Texas and Pennsylvania, we receive both federal and state subsidies.

**Long-distance services**

Long-distance services enable customers to make calls that terminate outside their local calling area. We offer a variety of long-distance plans, including an unlimited calling plan, and offer a combination of subscription and usage fees.

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**Data and Internet services**

Data and Internet services include revenues from non-local private lines (typically inter-city) and for providing access to the Internet and IPTV. We also offer a variety of data connectivity services, including Asynchronous Transfer Mode and gigabit Ethernet products and frame relay networks. In our Pennsylvania markets, we also provide virtual hosting services, collocation services and e-commerce enabling technologies.

**Other services**

Other services include revenues from telephone directory publishing, wholesale transport services on our fiber-optic network in Texas, billing and collection services, inside wiring service, and maintenance.

**Other Operations**

Prior to 2010, our Other Operations segment consisted of Public Services, Business Systems, Market Response (telemarketing and order fulfillment) ( CMR ), and Operator Services. In early 2010, we sold CMR. Also in early 2010, we made a decision to exit the Operator Services business, which we expect to be completed during the first half of 2010. Our on-going Other Operations segment consists of two complementary non-core businesses:

*Public Services* provides local and long-distance service and automated calling service for correctional facilities.

*Business Systems* sells and installs telecommunications equipment, such as key, private branch exchange (PBX), and IP-based telephone systems, to business customers in Texas and Illinois.

Our Other Operations segment generated approximately \$0.5 million of cash flows from operating activities for the years ended December 31, 2009 and 2008. As of December 31, 2009, Other Operations had total assets of approximately \$12.3 million.

**Wireless partnerships**

Wireless partnership investment income is included as a component of other income. This includes our limited partnership interests in Boulevard Communications, a competitive access provider, and five cellular partnerships: GTE Mobilnet of South Texas, GTE Mobilnet of Texas RSA #17, Pittsburgh SMSA, Pennsylvania RSA 6(I), and Pennsylvania RSA 6(II).

We own 2.34% of GTE Mobilnet of South Texas Limited Partnership ( Mobilnet South Partnership ). The principal activity of the Mobilnet South Partnership is providing cellular service in the Houston, Galveston, and Beaumont, Texas metropolitan areas. Because we have a minor ownership interest and cannot influence operations, we account for this investment using the cost basis; income is recognized only on cash distributions paid to us up to our proportionate earnings in the partnership. We recognized income on cash distributions of \$5.7 million from this partnership for the year ended December 31, 2009, and \$4.1 million for the year ended December 31, 2008.

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We own 17.02% of GTE Mobilnet of Texas RSA #17, which serves areas in and around Conroe, Texas. Because we have some influence over the operating and financial policies of this partnership, we account for the investment under the equity method, recognizing income based on the proportion of the earnings generated by the partnership that would be allocated to us. Cash distributions are recorded as a reduction in our investment amount. For the years ended December 31, 2009 and 2008, we recognized income from this partnership of \$4.0 million and \$2.6 million, respectively and received cash distributions of \$2.0 million and \$0.9 million, respectively.

San Antonio MTA, L.P., a wholly owned partnership of Cellco Partnership (doing business as Verizon Wireless), is the general partner for both GTE Mobilnet of South Texas and GTE Mobilnet of Texas RSA #17.

We own 3.6% of Pittsburgh SMSA, 16.6725% of Pennsylvania RSA 6(I), and 23.67% of Pennsylvania RSA 6(II) wireless partnerships, all of which are majority owned and operated by Verizon Wireless. These partnerships cover territories that almost entirely overlap the markets served by our Pennsylvania ILEC and CLEC operations. Because of our limited influence over Pittsburgh SMSA, we account for the investment using the cost basis. For the years ended December 31, 2009 and 2008, we recognized income on cash distributions from Pittsburgh SMSA of \$6.3 million and \$5.6 million, respectively. The Pennsylvania RSA 6(I) and RSA 6(II) partnerships are accounted for under the equity method. For the years ended December 31, 2009 and 2008, we recognized income of \$9.1 million and \$7.5 million, respectively, and received cash distributions of \$8.3 million and \$7.0 million, respectively, from these partnerships.

Boulevard Communications, L.L.P. is a Pennsylvania limited liability partnership equally owned by us and a company in the Armstrong Holdings, Inc. group of companies. Boulevard provides point-to-point data services to businesses in western Pennsylvania, including access to ISPs, connections to inter-exchange carriers, and high-speed data transmission. We account for the Boulevard investment under the equity method. Our investment in this partnership and the income/loss generated is immaterial.

*Customers and Markets*

Our Illinois local telephone markets consist of 35 geographically contiguous exchanges serving predominantly small towns and rural areas. We cover an area of approximately 2,681 square miles, primarily in five central Illinois counties: Coles, Christian, Montgomery, Effingham, and Shelby. We provide basic telephone services in this territory, with 63,866 local access lines, or 23.8 lines per square mile, as of December 31, 2009. Approximately 55.2% of our local access lines serve residential customers, with the remainder serving business customers. Our Illinois business customers are predominantly small retail, commercial, light manufacturing, and service industry accounts, as well as universities and hospitals.

Our 21 exchanges in Texas serve three principal geographic markets Lufkin, Conroe, and Katy in an approximately 2,054 square mile area. We provide basic telephone services in this territory, with 128,591 local access lines, or approximately 62.6 lines per square mile, as of December 31, 2009. Approximately 64.5% of our Texas local access lines serve residential customers, with the remainder serving business customers. Our Texas business customers are predominately manufacturing and retail industries; our largest business customers are hospitals, local governments, and school districts.

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The Lufkin market is centered primarily in Angelina County in east Texas, approximately 120 miles northeast of Houston, and extends into three neighboring counties. The area is a center for the lumber industry and includes other significant industries such as education, healthcare, manufacturing, retail, and social services.

The Conroe market is located primarily in Montgomery County and is centered approximately 40 miles north of Houston. Parts of the Conroe operating territory extend south to within 28 miles of downtown Houston, including parts of the affluent suburb of The Woodlands. Major industries in this market include education, healthcare, manufacturing, retail, and social services.

The Katy market is located in parts of Fort Bend, Harris, Waller, and Brazoria Counties and is centered approximately 30 miles west of downtown Houston along the busy and expanding I-10 corridor. Most of the Katy market is considered part of metropolitan Houston, with major industries including administrative, education, healthcare, management, professional, retail, scientific and waste management services.

The Pennsylvania ILEC territory covers 285 square miles and serves portions of Allegheny, Armstrong, Butler, and Westmorland Counties in western Pennsylvania. The southernmost point of the ILEC territory is 12 miles north of the city of Pittsburgh. We provide basic telephone services in this territory, with approximately 54,778 local access lines, or approximately 192.2 lines per square mile, as of December 31, 2009. Approximately 52.2% of our local access lines in this territory serve residential customers and the remainder service business customers. The CLEC operations expand south to serve the city of Pittsburgh and north to serve the city of Butler. The CLEC primarily targets small to mid-sized businesses, educational institutions, and healthcare facilities.

*Sales and Marketing*

**Telephone Operations**

The key components of our overall marketing strategy in the Telephone Operations segment include:

- Positioning ourselves as a single point of contact for our customers' communications needs;
- Providing customers with a broad array of voice and data services, and bundling these services whenever possible;
- Providing excellent customer service, including 24-hour, 7-days a week centralized customer support to coordinate installation of new services, repair and maintenance functions;
- Developing and delivering new services to meet evolving customer needs and market demands; and
- Leveraging our history and involvement with local communities and expanding Consolidated Communications and Consolidated brand recognition.

Our consumer sales strategy is focused on increasing our penetration of broadband services, including DSL, IPTV and VOIP, in all of our service areas. We are also focused on cross-selling our services, developing additional services to maximize revenues and increase revenues per user, and increasing customer loyalty through superior service, local presence, and compelling product offerings.



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Our Telephone Operations segment currently has three sales channels: call centers, communication centers, and commissioned sales people. Our customer service call centers serve as the primary sales channels for residential and small business customers. We also have a group of commissioned sales people, called our Feet on the Street team. This team canvasses our territories offering residential customers our full suite of products, leading with our triple-play bundled offering of voice, DSL, and IPTV services. In addition to being a strong sales point of contact, this sales effort also helps us to identify and address customer service issues, if any, on a proactive, face-to-face basis. This team of individuals can be scaled up or down to match our business needs, including, for example, if we launch a new product.

In both the ILEC and CLEC markets, we have sales teams led by a manager who has geographic market responsibility. Sales representatives/account managers support the existing base of larger business customers and new prospects. Individual sales representatives are responsible for the entire telecom product set, customize proposals to meet the customer needs (access lines, long-distance, Metro-Ethernet circuits, data connectivity, hosted VOIP and business systems) and in most cases are charged with retaining and growing the telecom services within their account base.

Our customers also can visit one of our communications centers to address various communications needs, including paying bills or ordering new service. We believe that customer availability to communication centers has helped decrease late payments and bad debt, and reinforces our local presence.

Our Telephone Operations sales efforts are supported by direct mail, bill inserts, newspaper advertising, public relations activities, sponsorship of community events, and website promotions.

Our Directory Publishing business is supported by a dedicated sales force, which is focused on each of the directory markets in order to maximize sales with both traditional print and online advertising products. We believe the directory business has been an efficient tool for marketing our other services and for promoting brand development and awareness.

Our Transport Services business has a sales force of commissioned sales people specializing in wholesale transport products.

### **Other Operations**

Each of our Other Operations businesses executes our sales and marketing strategy primarily through an independent sales and marketing team comprised of dedicated field sales account managers, management, and service representatives. Our executives enhance these efforts by attending industry trade shows and assuming leadership roles in industry groups including the U.S. Telecom Association, the Associated Communications Companies of America, and the Independent Telephone and Telecommunications Alliance.

### ***Information Technology and Support Systems***

Our information technology and support systems staff is a seasoned organization that supports day-to-day operations and develops system enhancements. The technology supporting our Telephone Operations segment is centered on a core of commercially available and internally maintained systems.

We have successfully migrated most of the key business processes from all of our previous acquisitions into a single company-wide system and platform, which includes common network provisioning, network management, workforce management systems, and financial systems. Our core systems and hardware platforms are readily expandable.

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*Network Architecture and Technology*

All of our local networks are based on Carrier Serving Area ( CSA ) architecture. CSA architecture allows access equipment to be placed closer to customer premises, which means customers can be connected to the equipment over shorter copper loops than would be possible if all customers were connected directly to the carrier's main switch. The access equipment is connected back to the main switch on a high capacity fiber circuit, resulting in extensive fiber deployment throughout our network, which enables us to provide broadband services in excess of 20 megabits per second ( mbps ) to our customers.

A single engineering team is responsible for the overall architecture and inter-operability of the various elements in the combined network of our Illinois, Texas, and Pennsylvania telephone operations. Our combined network operations center ( NOC ) in Mattoon, Illinois, monitors the performance of our enterprise-wide communications network around the clock and deals with customer-specific issues. We believe our NOC allows our Telephone Operations to maintain superior network performance standards using common network systems and platforms, which allows us to efficiently handle weekend and after-hours coverage amongst all of our markets and more efficiently allocate personnel to manage fluctuations in our workload volumes.

Our network is supported by advanced 100% digital switches, with a fiber network connecting 64 of our 65 exchanges. These switches provide all of our local telephone customers with access to custom calling features, value-added services, and dial-up Internet access. We have four additional switches: one that supports feature-rich VOIP, two dedicated to long-distance service, and one that supports our Public Services and Operator Services businesses.

In the past 10 years, we have invested over \$400 million to develop a high-quality 100% digital switching network, comprising 65 central offices and 482 CSAs. The CSA architecture has enabled us to provide DSL service, with speeds up to 3 mbps, to over 95% of our access lines. In addition, we have deployed fiber-optic cable extensively throughout our network, resulting in a 100% Synchronous Optical Network (SONET) that supports all of the inter-office and host-remote links, as well as the majority of business parks within our ILEC service area.

As a result of our advanced network, we introduced IPTV service in selected Illinois markets in 2005, Texas markets in 2006, and Pennsylvania markets in 2008. As of December 31, 2009, IPTV was available to approximately 188,000 homes in our markets. Our IPTV subscriber base continues to grow and now totals 23,127 subscribers as of December 31, 2009. We do not anticipate having to make any material capital upgrades to our network infrastructure in connection with the continued growth of our IPTV product except for providing set-top boxes to future subscribers and adding head-end equipment and capacity as we further increase our high-definition channel offerings.

We also operate a 2,000 mile fiber network in the State of Texas. Approximately 52% of this network consists of cable sheath that we own, either directly or through our majority-owned subsidiary East Texas Fiber Line, Inc. ( ETFL ). For most of the remaining route-miles of the network, we utilize strands on third-party fiber networks under contracts commonly known as indefeasible rights of use. We sell competitive wholesale capacity on this network to other carriers, wireless providers, CLECs and large commercial customers. In addition, this fiber infrastructure provides the connectivity required to provide IPTV, Internet and long-distance services to all Consolidated residential and enterprise customers.

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In Pennsylvania, we operate a CLEC with an extensive network consisting of over 557 route miles of fiber-optic facilities in the Pittsburgh metropolitan area. The CLEC has placed equipment in 27 Verizon central offices and one Embarq central office, and primarily serves its customers using UNE loops. In the Pittsburgh market, the CLEC operates a carrier hotel that serves as the hub for its fiber-optic network. We offer space in this carrier hotel to ISPs, long-distance carriers, other CLECs, and other customers who need a carrier-class location to house voice and data equipment and access to a number of networks, including ours.

*Employees*

At December 31 2009, we had 1,095 full-time and 118 part-time employees. Approximately 52% of our employees are covered by collective bargaining agreements as shown in the table below:

Location	# of Employees Covered	Union (1)	Contract Expiration Date
Illinois	340	IBEW	11/15/2012
Lufkin/Conroe, Texas	181	CWA	10/16/2010
Pennsylvania (ILEC)	66	CWA	09/30/2011
Katy, Texas	38	CWA	02/28/2011
Pennsylvania (CLEC)	11	CWA	02/29/2012
Totals	636		

## (1) IBEW

International  
Brotherhood of  
Electrical  
Workers

CWA  
Communication  
Workers of  
America

As a whole, we believe our relations with our employees are good.

We expect the number of employees to be reduced by approximately 75 full-time and 90 part-time positions as a result of the sale of CMR and our exit of the Operator Services business. See Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations Subsequent Events .

**Our Strengths***Technologically advanced network*

We have made significant investments building our technologically advanced telecommunications network. As a result, we are able to deliver high-quality, reliable video, data, and voice services in all of the markets we serve. Our wide-ranging network and extensive use of fiber provide an easy reach into existing and new areas. By bringing the fiber network closer to the customer premises, we can increase our service offerings, quality and bandwidth services. Our Internet Protocol ( IP ) backbone network provides a high-quality, flexible platform that allows us to deliver broadband applications to our customers at competitive prices. Approximately 95% of our total local access lines were DSL-capable as of December 31, 2009, and approximately 96% of these DSL-capable lines are capable of speeds of 3 mbps or greater. Metro-Ethernet, VOIP services, and other additional IP services leverage the extensive MPLS (Multi-Protocol Label Switching) core network, making it more efficient and scalable. Our existing network can support increased IPTV subscribers with limited additional network preparation thereby driving additional revenue

growth.

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*Attractive markets*

The geographic areas we serve are characterized by a balanced mix of growing suburban areas and stable, rural territories.

Our Lufkin, Texas, and central Illinois markets have experienced only nominal population growth over the past decade. As of December 31, 2009, 99,583, or 40.3%, of our local access lines were located in these markets. However, this low growth, low customer density and the predominantly rural residential character of these areas have historically discouraged competitors from making the significant capital investment required to offer competing services.

Our Conroe and Katy, Texas markets are suburbs of the Houston metropolitan area. As of December 31, 2009, 92,874, or 37.6%, of our local access lines were located in these markets. Conroe and Katy have experienced above-average population and business employment growth over the past decade as compared to the remainder of Texas and the United States as a whole. According to the most recent census, the median household income in the primary county in our Conroe market was \$50,000 per year, and \$60,000 per year in our Katy market. In contrast, the median annual household income was \$39,927 in Texas and \$42,148 in the United States.

Our Pennsylvania ILEC operates in a territory covering approximately 285 square miles, including portions of Allegheny, Armstrong, Butler, and Westmoreland counties in western Pennsylvania. Over the past decade, our ILEC territory has experienced population growth as the suburban communities in its territory have been expanding (the southernmost point of this territory is only 12 miles from Pittsburgh). For similar reasons, the ILEC has benefited from growth in business activity and favorable market demographics. As of December 31, 2009, 54,778, or 22.1%, of our local access lines are located in our Pennsylvania ILEC territory.

Our Pennsylvania CLEC assets provide telecommunications and broadband services south of our ILEC territory to customers in the metropolitan Pittsburgh area, and to the north of the ILECs territory in the City of Butler and surrounding areas.

*Broad product offerings and bundling of services*

We are able to leverage our long-standing relationship with our customers by offering them a broad suite of telecommunications and information services that enables us to pursue increased revenue per access line by selling additional services through a bundling strategy, that includes our triple play offering of voice, DSL, and IPTV services. Our residential and business customers have access to a broad array of competitively priced advanced television programming, data, and voice service choices with a single point of contact. In addition to providing local and long-distance telephone service, customers can choose multiple speeds of DSL service and IPTV programming with over 230 all-digital channels, 50 high-definition ( HD ) offerings, and digital video recorder ( DVR ) services. We also offer custom calling services, carrier access services, VOIP service to residential and business customers, and directory publishing.

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By bundling our service offerings, we are able to offer and sell a more complete package of services, which we believe simultaneously increases our average revenue per user ( ARPU ) and adds value for the consumer. We also believe that bundling leads to increased customer loyalty and retention. As of December 31, 2009, we had 56,856 customers who subscribed to service bundles that included local service and a selection of other services including custom calling features, DSL, and IPTV.

*Experienced management team with proven track record*

With an average of over 25 years of experience in both regulated and non-regulated telecommunications businesses, our management team has demonstrated that it can deliver profitable growth while providing high levels of customer satisfaction. Specifically, our management team has a proven track record of:

- Providing superior quality services to rural customers in a regulated environment;
- Implementing successful business acquisitions and integrations; and
- Launching and growing new services, such as DSL and IPTV, along with managing CLEC businesses and complementary services, such as transport, business systems and directory publishing.

*Generally supportive regulatory environment*

As a RLEC, we benefit from federal and Texas and Pennsylvania state subsidies designed to promote universal service , or widely available quality telephone service at affordable prices in rural areas. For the year ended December 31, 2009, we received \$34.6 million in payments from the federal universal service fund, \$16.2 million from the Texas universal service fund, and \$5.2 million from the Pennsylvania universal service fund. In the aggregate, these payments constituted 13.8% of our total revenues in 2009. For the year ended December 31, 2008, we received \$32.1 million from the federal universal service fund, \$17.9 million from the Texas universal service fund, and \$5.2 million from the Pennsylvania universal service fund. In the aggregate, these payments constituted 13.2% of our total revenues in 2008.

**Business Strategies**

*Increase revenues per customer*

We continue to focus on increasing our revenue per customer, primarily by improving our DSL and IPTV market penetration, increasing the sale of other value-added services, and encouraging customers to subscribe to our service bundles.

We now provide IPTV service in all of our markets. After making necessary upgrades to our network and purchasing programming content, we launched IPTV in our Pennsylvania markets in April 2008, four months after acquiring the company. All of our markets offer HD programming and DVR service that further increases our ARPU. As of December 31,

David Peter Wong

/s/ Tung Kuen Tsui

Director

September 30, 2008

Tung Kuen Tsui



**EXHIBIT INDEX**

<b>EXHIBIT NO.</b>	<b>DESCRIPTION</b>
3.1	Amended and Restated Articles of Incorporation (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 3.1)
3.2	Second Amended and Restated Bylaws (incorporated herein by reference to the Company's Form 10-KSB, dated March 31, 1999, Exhibit 3.1.II)
4.1	Specimen Certificate for Common Stock (incorporated herein by reference to the Company's Form 10-Q for the quarterly period ended December 31, 2006, dated February 13, 2007, Exhibit 3.1)
4.2	Form of Warrant (incorporated herein by reference to the Company's Form 8-K, dated February 16, 2007, Exhibit 4.1)
4.3	Warrant, dated February 22, 2007, to Belmont Capital Group Limited (incorporated herein by reference to the Company's Form 8-K, dated February 16, 2007, Exhibit 4.2)
4.4	Warrant, dated February 22, 2007, to CCG Elite Investor Relations (incorporated herein by reference to the Company's Form 8-K, dated February 16, 2007, Exhibit 4.3)
5.1**	Opinion of Thelen LLP
10.1	Redemption Agreement, dated December 28, 2006 (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 10.1)
10.2	Tax Indemnity Agreement, dated December 28, 2006 (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 10.2)
10.3	2006 Long Term Incentive Plan (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 10.3)
10.4	2006 Director Stock Plan, dated March 1, 2006 (incorporated herein by reference to the Company's Definitive Proxy Statement, dated November 27, 2006, Annex 3)
10.5	Equipment Mortgage Agreement between Chengtong and Raiffeisen Zentralbank Österreich AG, dated January 12, 2005 (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 10.4)
10.6	Mortgage Agreement on Immovables between Shanghai Tuorong Precision Strip Company Limited and Raiffeisen Zentralbank Österreich AG, dated January 12, 2005 (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 10.5)
10.7	Letter of Offer between Chengtong and Raiffeisen Zentralbank Österreich AG, dated October 14, 2004 (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 10.6)
10.8	Amendment No. 1 to Letter of Offer between Chengtong and Raiffeisen Zentralbank Österreich AG, dated December 28, 2004 (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 10.7)
10.9	Amendment No. 2 to Letter of Offer between Chengtong and Raiffeisen Zentralbank Österreich AG, dated May 10, 2005 (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 10.8)



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10.10	Amendment No. 3 to Letter of Offer between Chengtong and Raiffeisen Zentralbank Österreich AG, dated July 26, 2005 (incorporated herein by reference to the Company's Form 8-K, dated January 4, 2007, Exhibit 10.9)
10.11	Debt Reduction Agreement, dated February 13, 2007, by and among the Company, Wo Hing Li and Partner Success Holdings Limited (incorporated herein by reference to the Company's Form 8-K, dated February 13, 2007, Exhibit 10.1)
10.12	Deed of Release, dated February 13, 2007, from Wo Hing Li, in favor of the Company, Partner Success Holdings Limited and Shanghai Chengtong Precision Strip Co., Ltd. (incorporated herein by reference to the Company's Form 8-K, dated February 13, 2007, Exhibit 10.2)

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10.13	Amendment to the Debt Reduction Agreement, dated February 20, 2007, by and among the Company, Wo Hing Li and Partner Success Holdings Limited (incorporated herein by reference to the Company's Form 8-K, dated February 16, 2007, Exhibit 10.4)
10.14	Form of Stock Purchase Agreement, by and among the Company and the Investors, dated February 16, 2007 (incorporated herein by reference to the Company's Form 8-K, dated February 16, 2007, Exhibit 10.1)
10.15	Form of Limited Standstill Agreement (incorporated herein by reference to the Company's Form 8-K, dated February 16, 2007, Exhibit 10.2)
10.16	Form of Subscription Agreement, dated November 1, 2007 (incorporated herein by reference to the Company's Form 8-K filed on November 1, 2007, Exhibit 10.1)
10.17	Form of Placement Agency Agreement, dated October 31, 2007 (incorporated herein by reference to the Company's Form 8-K filed on November 1, 2007, Exhibit 10.2)
21	Subsidiaries of the Registrant (incorporated herein by reference to the Company's Annual Report on Form 10-K filed on September 15, 2008, Exhibit 21)
22	Published report regarding matters submitted to vote of security holders (Incorporated herein by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended December 31, 2006, dated February 13, 2007, Exhibit 99.1)
23.1**	Consent of Thelen LLP (included in Exhibit 5.1).
23.2**	Consent of Murrell, Hall, McIntosh & Co., PLLP, Independent Registered Public Accounting Firm
23.3**	Consent of Moore Stephens, Independent Registered Public Accounting Firm
24.1*	Power of Attorney (included on the signature page hereto).

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\* Filed herewith

\* Previously filed on September 15, 2008

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